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The Relics of Intervention:
5. New Deal Welfarism — **Clarence B. Carson** — **451**
The growing welfare burdens largely began in the New Deal of the mid-Thirties.

The Illusion of a Riskless Society — **Elgin Groseclose** — **464**
The risks increase as the government intervenes.

Rothbard's Liberty Reviewed — **John Hospers** — **468**
A critical review of "The Ethics of Liberty."

Mixed Economies a No-Man's Land — **Glenn L. Pearson** — **485**
In the war between freedom and slavery, political intervention tends to enslave.

Public Policy and the Free Economy — **Thomas J. DiLorenzo** — **492**
Only the free economy is capable of achieving equity and prosperity.

Book Reviews: — **510**
"The Subterranean Economy" by Dan Bawly

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Clarence B. Carson

THE RELICS OF INTERVENTION:

5. New Deal Welfarism

THE welfare state is largely a relic of the New Deal. That is, it was conceived, advanced, and articulated in particular programs during the 1930s. It is a relic of a depression-born animus to assert the power of the central government into the lives of Americans, of a faith in the beneficence of government intervention. For several decades before the Great Depression, reformers had been proclaiming the necessity for and desirability of government action on behalf of elements within the population. The depression provided an opportunity for them to use the power of government.

The welfare state began as an idea, of course. This idea, though it has long since become an assumption, still undergirds the welfare state. It is the belief that it is the duty and responsibility of government to provide for the economic well-being and security of the people, especially that portion of them most exposed in the modern world. It is premised upon the fact that government can confiscate wealth by taxation and redistribute it. Beyond that it can compel redistributions by legislation even when the wealth never enters government coffers, as by fixing a minimum wage, for example. By various means, then, government could provide for the well-being and security of the people. New Dealers not only implanted the general idea but also placed heavy emphasis upon the leadership of the Federal government in welfarism.

Historians often speak of two New Deals. The First New Deal is usually located primarily in the years 1933–1934. Its most characteristic feature was probably the National

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Recovery Administration (NRA) with its industrial codes and the impetus it gave to national planning within industries. In broad terms, the aim of the First New Deal was to stimulate recovery by cutting production, raising prices, and credit expansion. The Second New Deal is concentrated in the years 1935–1938. Industrial planning was sloughed off, and the emphasis shifted to even more direct government involvement in finding ways for protecting and aiding farmers, labor unions, and the poor more generally.

Actually, however, the New Deal cannot be broken up into any chronological pattern into which all the measures will fit neatly. For example, there is a continuity in the agricultural programs throughout the period that was broken only temporarily by Supreme Court decisions. National planning as an idea was never abandoned, though there were changes in emphasis. From the outset, too, there was a welfarist tint to the programs, although the emergency confronting credit institutions and national planning were in the forefront. But the shift toward the welfare state did become much more pronounced from 1935 onward. The most dramatic step in that direction was the passage of the Social Security Act in 1935. Not only was the measure clearly welfarist in character but also it was not a temporary or emergency measure. It would extend indefinitely into the future if it were not nullified or repealed.

Social Security

In his message to Congress recommending the passage of Social Security, Roosevelt declared that the main objective "was, and is, the security of the men, women, and children of the Nation against certain hazards and vicissitudes of life. This purpose is an essential part of our task."[1] He went on to enumerate the programs to be included in it:

> At this time, I recommend the following types of legislation looking to economic security:
>
> 1. Unemployment compensation.
>
> 2. Old-age benefits, including compulsory and voluntary annuities.
>
> 3. Federal aid to dependent children through grants to States for the support of existing mothers' pension systems and for services for the protection and care of homeless, neglected, dependent, and crippled children.
>
> 4. Additional Federal aid to State and local public-health agencies and the strengthening of the Federal Public Health Service. I am not at this time recommending the adoption of so-called "health insurance," although groups representing the medical profession are cooperating with the Federal Government in the further study and definite progress is being made.[2]

In later pronouncements, Roosevelt set forth in broad and compre-

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hensive terms the extent of his welfare aims. In his Second Inaugural Address, delivered in 1937, he declared: "In this nation I see tens of millions of its citizens . . . who at this very moment are denied the greater part of what the very lowest standards of today call the necessities of life." He saw, he continued, "one-third of a nation ill-housed, ill-clad, ill-nourished."

> It is not in despair that I paint you that picture. I paint it in hope—because the Nation, seeing and understanding the injustice in it, proposes to paint it out. We are determined to make every American citizen the subject of his country's interest and concern. . . . The test of our progress is not whether we add more to the abundance of those who have much; it is whether we provide enough for those who have too little.[3]

In short, not to put too fine a point upon it, he intended to use the power of government to see that the wealth was distributed to care for those who had the least.

A Question of Constitutionality

Before looking more closely at some of the acts by which the welfare state was established, the question of the constitutionality of all this effort needs to be examined. I do not raise the question of my own will, of course; it was a burning constitutional issue in the period 1935–1938. By 1936, there was every reason to doubt that much of the New Deal legislation would make its way successfully through the courts. During the years 1935–1936, lower court federal judges issued some 1600 injunctions preventing officials from applying New Deal laws. "At no time in the country's history," the *Harvard Law Review* opined, "was there a more voluminous outpouring of judicial rulings in restraint of acts of Congress than the body of decisions in which the lower courts, in varying degree, invalidated every measure deemed appropriate by Congress for grappling with the great depression."[4]

Moreover, beginning in January, 1935, the Supreme Court began to nullify major acts. In the next sixteen months, 10 major cases came before the court. "In eight instances the decision went against the New Deal. Stricken down in succession were Section 9(c) of the National Industrial Recovery Act, the N.R.A. itself, the Railroad Pension Act, the Farm Mortgage law, the Agricultural Adjustment Act, the A.A.A. amendments, the Bituminous Coal Act, and the Municipal Bankruptcy Act."[5] Of the acts challenged all the way to the Supreme Court, only the monetary acts of 1933 and TVA had survived.

Nor was most of this legislation struck down simply on technicalities. The gravest of constitutional objections had been raised in the court decisions. One history sum-

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marizes the objections this way: "First, the Court firmly rejected all attempts to extend federal authority over production. It denied in succession that interstate commerce, appropriations for the general welfare, or taxation could be used to this end. Second, the Court denied the constitutionality of legislative delegation to the executive on the scale attempted in the N.R.A. or the Guffey Act. Third, and more broadly, the Court refused to accept the conception of constitutional growth, either by evolution or through economic emergency."[6]

Not only had much of the legislation fallen, then, but there was good reason to suppose that such replacement legislation as the National Labor Relations Act and new legislation such as the Social Security Act would suffer a similar fate. As Schlesinger has said, "The succession of judicial vetoes in critical areas of federal action . . . seemed to express a clear determination on the part of the Court to nullify the New Deal."[7]

Attacking the Court

Ever since, most historians have laid the blame for this state of affairs on several members of the Supreme Court. They made what amounted to *ad hominem* attacks on those justices who took the most consistent positions about New Deal legislation. Their ire has been most often focused on Justices Willis Van Devanter, George Sutherland, James C. McReynolds, and Pierce Butler. While the following may not be quite typical of the attacks on these justices, it does illustrate the *ad hominem* character of them:

> The four stalwarts differ among themselves in temperament. I think that Mr. Justice Butler knows just what he is up to and that he is playing God or Lucifer to keep the world from going the way he does not want it to. Sutherland seems to me a naïve, doctrinaire person who really does not know the world as it is. His incompetence in economic reasoning is amazing. . . . Mr. Justice McReynolds is a tempestuous cad, and Mr. Justice Van Devanter an old dodo.[8]

Justice Owen Roberts, who usually sided with the above four and wrote some of the most ringing opinions, has not usually been treated with so much disdain by historians. Nor has Chief Justice Hughes, who was most apt to shift back and forth between groups. Historians have usually been unstinting in their praise of Justices Harlan Stone, Benjamin Cardozo, and Louis Brandeis, who usually dissented about the unconstitutionality of New Deal measures.

That way of treating it was an excellent ploy for evading the issue, of course. The question was not the competence of the Court to make decisions. At least, no such question was ever raised to the relevant level of initiating impeachment proceed-

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ings. The question was whether or not the New Deal legislation was authorized by and in keeping with the Constitution of the United States. If it was not, and the Supreme Court had made that determination about much of it before the end of 1936, then the New Dealers were guilty of transgressing the bounds of the Constitution. The plausible course would have been to blame them for contempt of the Constitution, not the Court for applying it.

Unprecedented Action

Several considerations make this the more plausible interpretation. In the first place, much of the New Deal legislation was either without precedent—decidedly different in important features from any passed theretofore—or applied government power to new areas. Such precedents as existed were mostly in emergency measures passed during World War I, and these were too shortlived to have undergone full court testing. (In any case, for wartime measures to serve as precedents, it would have been necessary to buy the analogy between war and depression.)

Second, the acts nullified were not based on powers enumerated with any explicitness in the Constitution. The New Dealers relied generally either on the interstate commerce clause or the power to tax for the general welfare, the vaguest and most imprecise authority. This is not prima facie evidence of their unconstitutionality, but it did mean that where they were foraging into new territory, they could expect sharp challenges.

Third, the weight of precedent, so far as there was any, and the tendency of court decisions over the years made the constitutionality of the New Deal legislation doubtful. For example, the courts had gone to great lengths over the years to limit, confine, and define the commerce power. In one great swoop, the New Deal acted to override these limits.

The Duty of the Court

The majority on the Supreme Court had moved resolutely and with careful deliberation to halt the intrusions and to affirm the constitutional limits on the government. As Justice Roberts said, in *United States v. Butler,* "The question is not what power the federal Government ought to have but what powers in fact have been given by the people." He explained the role of the Court this way: "The Constitution is the supreme law of the land ordained and established by the people. All legislation must conform to the principles it lays down. When an act of Congress is appropriately challenged in the courts as not conforming to the constitutional mandate the judicial branch of the Government has only one duty—to lay the article of the Constitution which is invoked be-

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side the statute which is challenged and to decide whether the latter squares with the former."[9]

President Roosevelt bided his time throughout the year, 1936, avoiding any public statements about court decisions. There was some talk of proposing constitutional amendments which would clearly provide the New Dealers the power to do what they wanted to do. But no such amendments ever made it off the drawing board. To have proposed the amendments would have been a tacit acknowledgement that the courts were right in their interpretation of the Constitution. To have stated in blunt constitutional language the powers sought would have been to expose the power grab involved. Had such amendments been proposed in 1936 they would almost certainly have provoked controversies which might have had political consequences unfavorable to Roosevelt and the Democrats. Besides, Roosevelt must have already had a different scenario in mind, one which would enable him to move from strength rather than weakness.[10]

At any rate, he waited until after the presidential election to make his move. He continued to push welfarist legislation, even to getting part of the Agricultural Adjustment Act, which had been nullified, re-enacted. It was not done under the old name, not yet, but this did not forestall charges that the New Dealers were acting in contempt of the Constitution. The election results provided him with the background for action. Roosevelt won a landslide victory; only Maine and Vermont went into the Republican presidential column. The Democratic majorities in both houses of Congress were overwhelming.

Still, Roosevelt moved secretly and deliberately. First, he gave his Second Inaugural Address with its vigorous call for government action to deal with the distress of one third of the nation. After that, work was begun in secret on a Judicial Reorganization bill which was sent to Congress February 5, 1933. A few days before that, Roosevelt held a gala dinner for the members of the Supreme Court, among others. No word had yet leaked about the forthcoming bill. Then, in the hours before the message and legislative proposal went before Congress, President Roosevelt called a special meeting of his cabinet and congressional leaders. He simply read his proposal to them and without significant discussion dismissed them.[11]

The Court Packing Scheme

The Judicial Reorganization bill quickly became known as Roosevelt's "Court Packing Scheme." It did indeed propose to enlarge the Supreme Court. In his message to Congress, Roosevelt emphasized the old age of most of those on the Court

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and the alleged inefficiency that followed from that. He proposed that when any federal judge reached the age of 70 and did not retire that the President be authorized to appoint another judge. For the Supreme Court, the number to be appointed was to be limited to 6 additional justices, so that the number could not go higher than 15 members of the Court. If a justice voluntarily retired at the age of 70, no additional member would be appointed, of course.

Roosevelt took the case to the American people. On March 9, 1937, in a Fireside Chat (radio speech), he set forth his grievances against the present Supreme Court. He charged that the "Court has been acting not as a judicial body, but as a policy making body." He made it clear that in his opinion it was some of the men on the Court that were making difficulties. "Our difficulty with the Court today," Roosevelt said, "rises not from the Court as an institution but from human beings within it. But we cannot yield our constitutional destiny to the personal judgment of a few men who, being fearful of the future, would deny us the necessary means of dealing with the present."[12] It was necessary, Roosevelt declared, "to take action to save the Constitution from the Court and the Court from itself."[13] The probable impact of such a direct assault by the President on a few men in a public speech could hardly be exaggerated. Moreover, it was made against men who, by tradition, could make no public answer.

Roosevelt's Interpretation

That Roosevelt held a different view of the Constitution and of the role of courts in its interpretation from that traditionally held either by the courts or the American people should be made clear. A Roosevelt biographer reports that when Roosevelt took the oath of office, a few weeks before the above events, it was administered to him by Chief Justice Hughes. The old Chief Justice "read the oath with slow and rising emphasis as he came to the words 'promise to support the Constitution of the United States.' Roosevelt gave the words equal force as he repeated the oath. At this point, he said later, he wanted to cry out, 'Yes, but it's the Constitution as *I* understand it, flexible enough to meet any new problem of democracy—not the kind of Constitution your Court has raised up as a barrier to progress and democracy.' "[14]

Roosevelt dropped hints as to his view of the Constitution rather than making a legal argument for it. He said that "we must have Judges who will bring to the Courts a present-day sense of the Constitution. . . ," courts which would take up their "high task of building anew on the Constitution 'a system of living

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law.' "[15] More specifically, he proposed a line the courts might take to validate welfare legislation. He noted that "In its Preamble, the Constitution states that it was intended to form a more perfect Union and promote the general welfare. . . . But the framers went further. Having in mind that in succeeding generations many other problems then undreamed of would become national problems, they gave to Congress the ample broad powers 'to levy taxes . . . and provide for the common defense and general welfare of the United States.' "[16]

Underlying Roosevelt's remarks was a theory, a theory known as legal realism. Legal realism may also be described as legal relativism. On this view, the law at any given time is relative to the conditions which prevail and the aims and purposes of those who expound it. Rather than being fixed by constitution makers and legislators, it is growing, expanding, and changing. The beliefs, ideologies, and predilections of those who expound the law are determinative. The ideals which had guided, or at least been claimed by exponents of, American jurisprudence over the years were given short shrift by legal realists. Here, for example, is a more recent statement by a legal realist of his attitude toward them:

> . . . In the interest-balancing procedure of constitutional adjudication, neutrality has no place, objectivity is achievable only in part, and impartiality is more of an aspiration than a fact. . . . In making choices among competing values, the Justices of the Supreme Court are themselves guided by value preferences. Any reference to neutral or impersonal principles is . . . little more than a call for a return to a mechanistic jurisprudence [which, he goes on to assert, never existed]. . . . Even in the often-quoted assertion by Mr. Justice Roberts about the duty of the Court to lay the statute against the Constitution to ascertain if the one squares with the other, one would indeed have to be naive to believe that this statement in fact described the process.[17]

It might be supposed that there would be no way for legal realists to distinguish between good laws and bad laws. That is not the case, however. A good law is one that is "progressive"; a bad law is one that is "reactionary." Of course, reformers had co-opted the idea of progress for themselves.

The Court Upheld

Roosevelt did not succeed in getting his plan for reorganizing the judiciary through Congress. He labored to do so through a rather lengthy session, for those days, but to no avail. The Senate Judiciary Committee recommended its defeat in the most vigorous language it could summon for a public document. The report declared that "This bill is an invasion of judicial power

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such as has never before been attempted in this country." So far as the majority of the Committee could see, "The only argument for the increase which survives analysis is that Congress should enlarge the Court so as to make the policies of this administration effective." Further,

> This is the first time in the history of our country that a proposal to alter the decisions of the court by enlarging its personnel has been so boldly made. Let us meet it. Let us now set a salutary precedent that will never be violated. Let us, of the Seventy-fifth Congress, in words that will never be disregarded by any succeeding Congress, declare that we would rather have an independent Court, a fearless Court, a Court that will dare to announce its honest opinions in what it believes to be the defense of the liberties of the people, than a Court that, out of fear or a sense of obligation to the appointing power, or factional passion, approves any measure we may enact. We are not the judges of the judges. We are not above the Constitution.[18]

The end did not come so dramatically as the Committee apparently hoped, but the bill did not pass.

But neither the stirring words of the Committee report nor the refusal of Congress to enact the bill into law came soon enough to bolster the Court. The barn door had been locked after the horse had been stolen. The Court had shifted its stance before these decisions had been made. Justice Roberts apparently succumbed to Roosevelt's pressure on the Court and changed sides. Chief Justice Hughes, who had wavered back and forth in any case, went along with him to form a new majority on the Court. In March, 1937, the new majority on the Supreme Court sustained a Washington minimum wage law, reversing its position in a New York case made only the year before. In April, the new majority on the Court sustained the National Labor Relations Act in a series of decisions. In May, the Court sustained significant portions of the Social Security Act.

In short order, too, the slim majority on the Court was broadened. Beginning with the retirement of Justice Van Devanter in May, 1937, most of the older justices retired or died over the next couple of years. They were usually replaced by such known New Dealers as Hugo Black, William O. Douglas, and Felix Frankfurter. Roosevelt had lost the battle for court reorganization but won the war for a Court that would sanction New Deal legislation.

Bending the Constitution

An historian of the New Deal has said, "On the whole, the Founding Fathers sought to contain government, not promote change. It was remarkable that the New Deal was able to break through these carefully devised constitutional barriers for so long." [19] I quote the above two sentences because they place the

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emphasis where it belongs, not upon the Courts but upon the Constitution. After all, the Supreme Court survived the assault, indeed, survived and prospered. But the breaking of the barriers in the Constitution to the establishment of a welfare state is a different matter. The New Deal assault was like punching holes in a dam. Over the years, the holes have widened, so that more and more legislation, much of it not authorized by any stretch of the imagination by the Constitution, could get through.

That the clauses referring to the "general welfare" were grants of power to do anything, much less establish a welfare state, is highly doubtful. The reference to the "general welfare" in the Preamble is not a grant of power. It is a part of the statement of the purpose of the government being established. The phrase occurs again in the first clause of Article I, Section 8. It reads, "The Congress shall have Power To lay and collect Taxes, Duties, Imposts and Excises, to pay the Debts and provide for the common Defence and general Welfare of the United States. . . ." The most plausible interpretation is that the phrase is a limitation of the taxing power. Specifically, the term "general" is a limitation. That is, it is the *general* welfare for which taxation is authorized, not the local welfare or that of some special class or group of people. In any case, "welfare" did not then have the connotation that it has had since the New Deal.

Using the Power of Government to Redistribute Wealth

The most characteristic economic feature of welfarism is the use of the power of government to redistribute wealth. It is true, of course, that any government activity may result in the incidental redistribution of wealth. But it becomes welfarist activity when the main purpose is to transfer wealth from one group or class to another.

The Revenue Act of 1935 signaled the welfarist direction, though it was not the first measure that year of this character. In his message to Congress asking for increased taxes, President Roosevelt made the aim of redistribution clear. He said, "Our revenue laws have operated in many ways to the unfair advantage of the few, and they have done little to prevent an unjust concentration of wealth."[20] The revenue measure that was passed was blatantly discriminatory toward those with greater wealth. It increased the surtax on individual incomes over $50,000; the tax on incomes over $1 million was graduated steeply upward to 75% for all income over $5 million. Estate and gift taxes were increased. Taxes on small corporations were lowered slightly, while the rates on corporations with incomes over $50,000 were

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Lack of Purchasing Power

IN the early Nineteen Thirties, in the depth of the Great Depression, the theory became fashionable that the cause of all depressions was Lack of Purchasing Power. The people just did not have enough money, and because of unwarranted pessimism they were refusing to spend enough even of what they had. The solution was therefore simple: at such a time the government should boldly increase its own spending, "prime the pump," and "get things moving again."...

Unless there were some serious lack of coordination among prices, costs, and wages, mass unemployment would not exist in the first place. When it does exist, the only appropriate cure is individual adjustment of prices, costs, and wages to each other—the return of coordination. But this can be brought about automatically only if the competitive forces of the market are given free play.

HENRY HAZLITT, *Man vs. the Welfare State*

raised. Taxes were also levied on profits above 6%.

The largest scale redistribution effort in 1935 was undertaken under the Works Progress Administration (W.P.A.). It was set up under the Emergency Relief Appropriation Act passed in April, 1935. Harry L. Hopkins, an administrator with considerable experience already in spending money, was placed in charge. Hopkins had said on one occasion, "Why accept the evil of poverty? . . . I believe they are poor because we haven't wit and brains enough to divide up our national income each year so they won't be poor."[21]

At any rate, the WPA plunged vigorously into work relief programs. In the course of its career, nearly $11 billion was spent on 1,410,000 projects on which 8½ million different persons were employed. Although much of the WPA work was done on projects which are customarily in the domain of government, such as building roads and bridges, its primary purpose was the transfer of wealth to those reckoned to be needy. A means test was applied in the selection of workers, which certainly would not have been the case if the projects were the main concern. Moreoever, much, probably most, of the building was on projects ordinarily financed by local and state governments.

A Resettlement Administration was set up in May, 1935, to move destitute families into new areas and foster subsistence homestead communities. (This was one of Roosevelt's pet projects, enlivened by the idea of moving urban inhabitants to family farms, and such like. In the main, it provided temporary dwell-

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ings for transients.) In the same month, the Rural Electrification Administration was organized to make electricity available by low interest loans to isolated rural areas. A National Youth Administration, created by executive order in June, 1935, made jobs for young people, especially for those in schools and colleges needing part-time work.

The NLRA

It might not appear, on first examination, that the National Labor Relations Act, passed in July, 1935, was a redistribution program. This act, however, completed the work of empowering labor unions begun under the National Recovery Act. It placed the power of government behind the organization of labor unions, mainly by way of the National Labor Relations Board, weighted the legal scales in favor of unions, and signaled a determination by the federal government that unions should prevail. Thereby, unions were able to extort higher wages from employers than they could have received in the market. The differential is a redistribution of wealth from employers to employees.

The provisions of the Social Security Act have already been alluded to. Social Security redistributes wealth in several ways. First, unemployment compensation is financed by a payroll tax on employers. When it is paid out as unemployment compensation, it is a compulsory redistribution from employers to employees. For most of the old age and survivors program, employers are taxed an equal amount to that of the employees. This is a forced transfer from employers to employees. Moreover, although there is a Social Security fund into which receipts go, current benefits have been taken increasingly from current receipts. Hence, the program has become virtually a device for transferring wealth from those presently working to retirees and their survivors. (That is not to deny, of course, that those who contributed in the past have a just claim to some benefits.) Also, the act authorized treasury payments to aid states with old age pensions and for various classes of disabled persons.

Other Interventions

Welfare programs continued to proliferate through 1938, as new ones were regularly added. The Revenue Act of 1936 placed a tax on undistributed corporate profits. The Soil Conservation and Domestic Allotment Act of the same year paid farmers to take land out of cultivation. This was a transfer from taxpayers generally to farmers who complied with the program. The National Housing Act of 1937 provided low interest loans to public authorities for slum clearance and the building of low rent housing. It also

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provided rent subsidies for the tenants. Finally, the Fair Labor Standards Act of 1938 required employers to pay minimum wages for work during a maximum 44-hour week (any work beyond that amount would have to be compensated at a higher rate), and forbade child labor. So far as wage rates were higher than they would have been in the market, this was a forced transfer of payments from employers to employees.

The welfare state, then, is a relic of the New Deal. The rudiments of it were established during the years 1935–1938. It is a relic of the determination to use the power of government to redistribute and transfer wealth. It is a relic of the New Deal thrust to centralize and concentrate government power. Above all, the welfare state is a relic of the use of political strength to overawe the Federal courts and secure their enforcement of welfare and other legislation. Since the days of the New Deal many new welfare programs have been added and others expanded. Entitlements have now reached such a level that the budget is virtually out of control, and social programs are a huge burden on the economy.

Next: *Conclusion: The Relic of an Idea.*

—FOOTNOTES—

[1]Franklin D. Roosevelt, *Nothing to Fear,* Ben D. Zevin, ed. (New York: Popular Library, 1961), p. 55.

[2]*Ibid.*, p. 57.

[3]*Ibid.*, p. 105.

[4]Arthur M. Schlesinger, Jr., *The Politics of Upheaval* (Boston: Houghton Mifflin, 1960), p. 447.

[5]Alfred H. Kelly and Winfred A. Harbison, *The American Constitution* (New York: W. W. Norton, 1955, rev. ed.), p. 728.

[6]*Ibid.*, p. 744.

[7]Schlesinger, *op. cit.*, p. 452.

[8]Quoted in *ibid.*, p. 457.

[9]Henry S. Commager, ed., *Documents of American History,* vol. II (New York: Appleton-Century-Crofts, 1963), p. 249.

[10]See James M. Burns, *Roosevelt: The Lion and the Fox* (New York: Harcourt, Brace and Co., 1956), p. 295.

[11]See *ibid.*, pp. 293–94.

[12]Roosevelt, *op. cit.*, p. 115.

[13]*Ibid.*, p. 112.

[14]Burns, *op. cit.*, p. 291.

[15]Roosevelt, *op. cit.*, pp. 112, 114.

[16]*Ibid.*, p. 110.

[17]Arthur S. Miller & Ronald F. Howell, "The Myth of Neutrality in Constitutional Adjudication" in *Judicial Review and the Supreme Court,* Leonard W. Levy, ed. (New York: Harper Torchbook, 1967), pp. 212–13.

[18]Ray A. Billington, *et. al.*, eds., *The Making of American Democracy,* vol. II (New York: Holt, Rinehart and Winston, 1962), p. 338.

[19]Alonzo L. Hamby, "Introduction" in *The New Deal* (New York: Weybright and Talley, 1969), p. 8.

[20]Quoted in Richard B. Morris, ed., *Encyclopedia of American History* (New York: Harper & Bros., 1953), pp. 352–53.

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Elgin Groseclose

The Illusion of a Riskless Society

THROUGHOUT history the fear of insecurity, from floods or famine, from enemies without or within, has driven mankind to erect barriers against the onset of disaster. Throughout history also such barriers—from the barns that led the man of the parable to tell his soul to take its ease, to the walls that cities have built that eventually fell to some invader—have proved illusory. In this country, protected as it is by the barriers of two great oceans, the search for security is no less fear-driven, but its direction, in an increasingly monetized society, is in a search for bastions. And since this is an increasingly socialized society, a chief aim of political policy has been to provide, through governmental agencies and power, what is currently referred to as a "safety net" for every citizen.

Yet as we may observe, the search for such security has proven illusory—mainly because of decay of its fabric, that is, the monetary standard of which the net is woven. We may review a number of these efforts by government.

First Effort—Riskless Banking

Throughout the latter decades of the nineteenth century, "check book money" came into increasing use as a medium of payments. But check book money depended upon the solvency of the bank in which the real money was deposited. Bank failures became a periodic feature of economic history.

In 1913, following the "rich man's panic" of 1907, the result of overspeculation and bank failures, public outcry for a "flexible currency" brought forth the Federal Reserve System designed, in the words of the Secretary of the Treasury, to "make panics mathematically impossible." Banking was to be made riskless for both banks and depositors by allowing overshot banks with cash shortages to trade collateral for legal tender currency at the Reserve banks. With this assurance of liquidity, banks were now allowed to reduce their capital reserves against deposits from a standard 25 per cent to a sliding scale down to 12 per cent

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and as low as 5 per cent on time deposits. Under subsequent legislation and regulations, also, banks were able to shift more and more of their assets from short term self-liquidating commercial paper to long term mortgages and bonds, thereby impairing their liquidity and ability to meet sudden withdrawals.

This effort to create riskless banking collapsed in the securities market panic of 1929 which led to the bank "holiday" of 1933 when every bank in the country was forced to close its doors.

Second Effort—Riskless Deposits

The country now concluded that, however feeble the banks might be, whatever extravagant lending they might indulge in, their customers, at least the smaller ones, should be protected and their deposits made riskless. This led to the enactment in 1933 of deposit insurance legislation by which eventually two mammoth government corporations, the Federal Deposit Insurance Corporation and the Federal Savings & Loan Insurance Corporation, were set up "to restore confidence in the banking system and protect depositors."

By 1979 the futility of this effort became evident to the bank regulators. Thus, in 1979, William M. Isaac, president of the FDIC Corporation, pointed out that the risk assets of the banking system—total assets less cash and equivalents—had risen from 22 per cent in 1945 to 80 per cent by 1978. He commented ominously, "One would think that with banks assuming greater risks, and the economy more volatile, capital ratios would be increasing. Just the opposite." He cited that equity to risk, that was around 30 per cent in 1900, had dropped steadily to around 8 per cent in 1978.

Today the cause for concern is greater. *The New York Times* for January 25, 1982, noted that of the 15 largest bank holding companies, the equity to assets ratio ranged from 4.55 per cent to as low as 3.25 per cent; and we may add that if bankers' portfolios were valued at market, the result in many cases would be a negative ratio. Take, for instance, a Aaa bond like AT&T 7s of 2001, issued in 1971 at 99.25, that has sold recently for as low as 50.

Presently the savings and loan associations are approaching crisis under the necessity of borrowing at rates up to 15 per cent against mortgage assets acquired when rates were as low as 8 per cent; and each day brings reports of new mergers and take-overs to save failing associations from outright default. The most recent merger was reported on March 24, 1982, "to avert what would be the biggest bank failure in the nation's history."

With customers' deposits now guaranteed up to $100,000, the $8 billion insurance fund of the two

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corporations has become totally inadequate as guarantee. This has led to legislation to back up deposits by the "full faith and credit of the U.S." regardless of the adequacy of the insurance fund. A bill to this effect was passed by the House with only 10 minutes of debate; its fate in the Senate has not (at this writing) been resolved. Other proposals are for the government to subsidize $210 billion in old low-interest mortgages by paying half the difference between the yield and the market rate on current deposits—a procedure that *The New York Times* estimates could cost the taxpayers from $4 to $5 billion a year for many years.

Third Effort—Riskless Aging

In 1933 the government undertook to guarantee income for the aged through a Social Security system by which a percentage levy was laid on earned income, the proceeds of which were invested in government bonds, from which payments were made as the contributor reached retirement age. Starting out at a modest percentage of earned income, the levy has steadily increased to a 1981 tax of 9.3 per cent on income up to $29,700. Since the tax receipts were invested in government bonds, for nearly 50 years the system has been a means of covering federal budget deficits; today, however, due to steady increase in benefits, the system is facing bankruptcy unless relieved by further taxes either from the income contribution or general revenues.

When Joseph foresaw a famine in Egypt he stored harvest surpluses of the good years in granaries against the years of dearth. Such a method is impossible today in a system of debt money. Who is to provide cash against the bonds but the very ones who are in need?

Fourth Effort—Riskless Prices

Since 1922 government policy has been to stabilize prices in order to protect producers of goods and services from loss from price fluctuations. This is theoretically achieved by the Federal Reserve System in buying and selling government bonds to provide an even supply of money. But the essence of trade is differences in prices. If all prices were stable, enterprise would wither, as the effect of rent control on housing supply has demonstrated. If modern technology means anything it is to make goods cheaper.

The secular effect of the policy of maintaining prices has been a steady increase in prices, with the increase steadily accelerating until it reached double-digit rates in 1980 and produced a voters' revolt.

Fifth Effort—Riskless Money

All the efforts to remove risk from banking, from livelihood, from enterprise have been, as we have noted, through the agency of money. Money

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is the foundation stone in the wall of security. But money, no longer a substance, like gold or silver, but an I.O.U. of the Federal Reserve System, a note without maturity, melts away like shifting sand under the cyclical rainfall of business.

The last element of substance in money disappeared in 1971, when the "gold window" was finally closed on international holders of dollars. Since then, holding money has become the greatest risk of all. This has become evident in the rising interest rate demanded by lenders to offset the erosion of the dollars due them. This rise in interest rates has been going on for the past 40 years, generally unperceived until the last decade.

Sixth Effort—Speculation

The disappearance of financial stability has led inevitably to a surge of speculation and gambling. As the Minority Report of the Gold Commission points out, scheming, speculation, and sophisticated tax avoidance have replaced productive effort, savings, and planning for the future.

Trading in currencies, the Report adds, has become more rewarding to banks than conventional business of brokering loans from savings. The futures and options market has turned into a giant gambling game. Futures are sold in currencies, and more recently futures and options on stock-indexes. In 1980 more futures on Treasury bonds were sold on the Chicago Board of Trade than on cattle. Billions of dollars are obtained from banks by corporations for the purpose of "take-overs" of other corporations with no indicated purpose of developing new industries or sources of basic wealth. Gambling has become a state enterprise. Illegal for individuals, in 1980, over $2 billion was gained from official lotteries for the benefit of state governments.

The High Road to Stability

Despite the evidence of an increasingly unstable society due to the monetary standard in which business is done—despite also a so-called "tight money policy" by the Federal Reserve—the printing press continues to roll and the amount of debt on demand continues to rise. Between February 28, 1981, and February 28, 1982, corresponding closely with the first year of the Reagan Administration, the legal tender circulation increased from $131,862 million to $140,525 million, while the demand debt of the Federal Reserve bank and banking system (called M_1) rose from $424 billion to $447 billion. Since none of this debt is dischargeable in any legal tender but irredeemable paper, it is obvious that until the powers of the Federal Reserve to create fictitious money are curtailed, no degree of stability will be achieved.

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John Hospers

Rothbard's Liberty Reviewed

The Ethics of Liberty by Murray Rothbard. (Atlantic Highlands, N.J.: Humanities Press, 1982), 268 + x pp., $15.95 hardbound.

THE long-awaited capstone to Professor Murray Rothbard's series of books on political economy has at last appeared. His earlier two-volume work, *Man, Economy, and State,* was a systematic defense of free-market economics. His *Power and Market* was a defense of laissez faire capitalism against numerous objections. The present volume contains his political-legal philosophy. The word "ethics" in the title is not quite appropriate, since the author does not attempt to discuss matters of good and bad, right and wrong; what he does undertake to discuss is what kind of actions should be prohibited and why.

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The Natural Law Tradition

The first four chapters give an all-too-brief account of the philosophical underpinnings of the political philosophy that follows. The author anchors his views in the "natural law" tradition set forth most forcefully by Thomas Aquinas, but developed here without Aquinas' theological framework. The crucial terms here, "man's nature" and "natural law," require more analysis than the author gives them. Just as it is cat-

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nature to purr, dog-nature to bark, and the nature of both to prowl, so it is man's nature to use his rational powers: to form concepts, to integrate them, to make decisions, to plan for the future.

Many questions arise, however, as to the meaning of the word "nature" in this context. (1) In one sense, "the nature of X" means whatever characteristics are defining of X; thus, the "nature" of gold is stated when one lists the characteristics which define gold, those without which something would not *be* gold. Out of this arise numerous philosophical questions, such as the difference between "would not be gold" and "would not be *called* 'gold,' " and with it the whole question (not discussed here) of whether all definitions are linguistic conventions or whether there are in some sense "true definitions." (2) In any case, the phrase "the nature of" is generally used more widely than to include only defining characteristics. "It is in the nature of cats to purr" could still be true even though some cats never purr, while yet continuing to be cats. Similarly, a person may be or become a "human vegetable" while yet remaining a human being. (This is the basis for the defense of a *biological* definition of "man" in terms of physical features that distinguish human beings from all other animals—a kind of definition Rothbard does not discuss.)

In any event, I believe that the phrase "the nature of," at least when applied to living things, is used to refer to fundamental dispositions to act and respond in certain ways. To call them *dispositions* is not to imply that they will always be actualized: to say that lions are disposed to hunt (whether or not this is defining of lions) is to say that they as a species possess this tendency, even though (as when they are fed all their meals in a zoo) they never actually exhibit hunting-behavior. And to call them *fundamental* means that other dispositions can be explained in terms of them: thus, Bergson's definition of man as "the laughing animal" may uniquely identify man, but is less fundamental than the definition "the rational animal," since if a person lacked the intelligence to appreciate a humorous situation he would not laugh.

The term "rational" is a somewhat slippery one, as illustrated by countless questions in ethics such as "It may be *right* to rescue a child from a burning building, but is it *rational*?" One manifestation of rationality, but not the only one, is presumably reason*ing*. But even this relatively clear component of "reason" is not clearly unique to the species we call man: Don D. Davis has given considerable evidence in his book *The Unique Animal* that some other creatures, such as chimpanzees, have the capacity to engage in

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elementary forms of reasoning. For this reason he defines man in terms of (1) the ability to *symbolize* (to decide to assign a relationship between two dissimilar and previously non-contiguous events), and (2) the ability to *hypothesize* (to propose a relationship or connection between two or more non-contiguous events). No other creature on earth, he says, has these two abilities.

Neither does the term "natural law" bear its meaning on its face: it is conceived quite differently by those in the tradition of Aquinas from what it is by certain contemporary legal scholars, e.g., Theodore Benditt in *Law as Rule and Principle*. The *content* of what is allegedly known by insight into "natural law" is far from clear.

Rothbard's example of wanton killing (at least within the tribe) being wrong is an unusually safe one: this is one of the few examples of a moral rule that would be upheld in virtually any society and on practically every ethical theory; in any case, a killing that one would wish to defend would not be called "wanton," just as a killing that one considered justifiable would not be called "murder." But when we leave these "safe" examples, what specific rules of conduct does natural law enjoin or prohibit? Does it permit adultery? abortion? euthanasia? Does it insist on "one husband, one wife"? Does it prohibit cruelty to animals? It is far from clear what tenets allegiance to "natural law" commits one to. Nor will any reference to "an objective moral order" (p. 11), at least without coming to grips with the many overlapping meanings of "objective" in this context, help to fill the gap.

All Rights as Property Rights

Then follows a lengthy discussion of rights. The term "a right" is neither defined nor distinguished from related terms such as "a liberty," but the philosophical literature on such definitions and distinctions is already endless. Instead, Rothbard comes at once to his most original and distinctive thesis: that all rights are reducible to property rights. For example, a person does not have the right of freedom of speech on another's property, e.g., to shout "Fire!" in a crowded theater or to shout obscenities in a cathedral. Most writers who insist on freedom of speech as a right have not been much bothered by considerations of property, and Rothbard "sets them straight" with clarity and elegance.

Whether free speech is limited solely by property rights, as Rothbard contends, will be a matter of continuing controversy. For example, (1) courts have held that distribution of leaflets in a company-owned town should be permitted even though the company objects, because of the importance of the dissemination of knowledge and opin-

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ion. Nor would everyone agree that all forms of speech, even on one's own property, should be permitted: (2) If you gather a group together on your yard, across the street from a factory, all shouting "Burn the factory down!" most courts would call this incitement to riot (as did Mill), although Rothbard contends (p. 80) that " 'inciting to riot' is a pure exercise of a man's right to speak."

Questionable Premises

In order to preserve the thesis that all rights are property rights, Rothbard must interpret the concept of property in certain ways which, according to some critics at least, involves making square pegs try to fit round holes. Thus, (1) since crimes against persons (murder, rape, battery, etc.) are to be condemned as much as crimes against property such as burglary and theft, one must accept the Lockean view that "every man has property in his own person." But many writers have argued at length that ownership is a relation between a person and something *other* than that person, in which case one cannot speak of *self*-ownership.

Moreover, (2) There are some kinds of activity which the laws of virtually every nation have declared punishable although they do not fall under the heading of property, such as libel, slander, and blackmail. One's reputation, says Rothbard, is not one's property, and thus anyone should be free to say about you whatever they like. By contrast, violation of patent and copyright *is* a violation of one's property rights (one's right to reap the fruits of one's labor) and should be prohibited. Many persons will not see that sharp a difference between the two classes of offenses. Even though the book you have written is your property and your reputation (as opposed to your character) is not, allegations falsely made about you by others may cause you greater harm (e.g., the loss of your job) than loss of your material possessions. And it could reasonably be contended that all infliction of *harm* on one person by another should be forbidden.

> . . . a man may rightly come to own previously unowned land by "mixing his labor" with it.

Rothbard defends the Lockean view on property rights in land: that a man may rightly come to own previously unowned land by "mixing his labor" with it — "the homestead principle." (Georgists allege that persons may own the crops grown on land but not the land itself, which is of course an invitation for government to claim ownership of the land — a position against which Rothbard argues effectively.) Many persons who would agree that one

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should own previously unowned land if he clears the forest, tills the soil, and plants crops on it, would not agree that he should own it if by accident he has merely *found* something (e.g., valuable minerals) on it. Rothbard argues effectively against this position as well: if the finder has no right to it, who does?

But there are many other cases, which he does not discuss, in which the answer is not so clear. (1) What if a man does *nothing* to a piece of wilderness land but chooses to keep it in its wild state, defending it against trespassers with guns or trained dogs? (2) What if he runs around a piece of land twenty times without stopping? Has he "mixed his labor" with it then? (Need it be "socially useful" labor like agriculture?) (3) What if he does nothing to the land but purifies the polluted air above it? Does this entitle him to nothing? (4) What of riparian rights? How is the dispute to be settled between residents of California and Arizona as to whether both may use the waters of the lower Colorado River? Can anyone take what he likes where he likes, or can a man own a section of the river and drain it all off for himself, so that there is only a dry bed downstream? (5) Can one own a section of ocean by fishing in it or traversing it with a boat? Or, to use Robert Nozick's example, if a man owns a can of tomato juice and pours it into the ocean and waits till it has dispersed, can he claim ownership of the ocean (provided it was previously unowned)? (Rothbard discusses some aspects of ownership of bodies of water in his *Power and Market.*)

Possible Exceptions

Even over what is clearly one's own property, one does not have the right of unlimited use or control. A man does not have the right to lure people onto his property, kill them, and bury the bodies in the basement. This, of course, violates their right to "property in their own persons." There are many other problems about what you may do with your house or yard: may you surround it with a moat containing piranhas, or set up an electrified fence that will kill attempted trespassers? May you build your house uphill from another, so that when the rains come the property below will have mud slides?

Do policemen have the right to enter the property "on suspicion"? Rothbard says that if they do enter it and don't find the evidence that will incriminate, they should themselves be subject to arrest. I submit that if policemen were hamstrung by such a requirement, few crimes would be solved: that in the interests of finding the guilty party the owner does not have the right to forcibly evict them, and even if it turns out that the suspect is not guilty they should not be subject to

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prosecution for making a reasonable mistake. If the guilty party is not Jones but Jones' identical twin, should policemen really be prosecuted for stopping and searching Jones in the reasonable belief that they are apprehending the twin?

Nor, I would add, should a man have the right to use his property in such a way as to expose others to unreasonable *risk*. Should you be permitted to raise poisonous snakes in your back yard in the city? Is it really necessary for neighbors to wait until one of them has been bit? A person, as the owner of his own body, may take any kind of risk for himself alone; but the exposure of others to risk is surely a proper matter for legal prohibitions. Should a man be permitted to manufacture atomic bombs in his basement? or poison gas? (One wonders whether Rothbard would use the criterion of negligence or that of strict liability in such cases—an extremely important issue which remains undiscussed.)

Laws regarding the *transmission* of property—by sale, gift, or bequest—are well discussed by Rothbard. If Jones' heirs claim property that has been seized from Smith and is now occupied by Smith's heirs, Jones' heirs have the right to dispossess Smith's heirs of it, minus whatever movable additions and improvements Smith's heirs have made to it. The conditions under which Jones is entitled to *be* an owner, however, are not always so clear. Should the present inhabitants of the United States be required to return the land to the Indians, who had it first? Or should such claims be denied on the ground that the Indians—most North American Indians, at any rate—did not really *reside* in a certain place and grow crops there, but were nomadic, wandering about from one area to another, staying in one place only as long as the hunting and fishing was profitable and then moving on? Hunting requires labor; does that labor constitute ownership—of the animals only, or of the land as well?

The Right of Self-Defense

That a person has the right of self-defense against aggression (as well as the right to defend *others* against aggression if he chooses) seems clear enough. What is less clear is the extent to which he is entitled to respond to *threats* of aggression. If a man looks at you threateningly and moves to pull out what you *think* is his knife, have you the right to take a pessimistic view of his intentions and attack him first (the "pre-emptive strike" problem)? Since most threats are not followed through, you presumably have no right to kill a man just because he says "I'll kill you," but at what point *do* you have the right to kill him, under the heading of self-defense?

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These are important and troublesome questions to which neither Rothbard nor anyone else has presented clear-cut answers. But I would make the point that it is not necessarily *physical* aggression or threat thereof to which one's right to self-defense is limited. If a man continually baits you, calls your wife a whore, or shouts that he has just raped her, and you finally take a swat at him, are you guilty because you started the *physical* fight? Might he not be called the initiator even though his aggression was only verbal? This is surely clear in the case of theft: you catch a man stealing your tape-recorder and you forcibly take it back from him. You started the physical confrontation; *he* was only peacefully taking what belongs to you. The same point could be made concerning trespass—and possibly also the breaking of contracts. There are many forms of aggression, and many proper (and many improper) forms of retaliation.

That punishment should be "proportional to the offense" is a principle Rothbard defends at some length, and quite rightly: you shouldn't be permitted to shoot dead the neighbor boy who is stealing a watermelon from your garden. But there is much dispute as to which offenses are the most serious and therefore merit the most serious punishment. Offenses against a person aren't *always* worse than offenses against property—many people would rather be mauled or lose an ear lobe than lose a precious heirloom or their cache of gold.

Most troublesome of all are those cases in which damage or injury has been inflicted but the inflictor had no guilty intent.

Most troublesome of all are those cases in which damage or injury has been inflicted but the inflictor had no guilty intent. Cases of accidental injury or damage are far more frequent than those intentionally administered, and the criteria for punishment much less clear. One wonders what Rothbard would do with "Typhoid Mary" cases: the women were carriers of a lethal disease, and communicated it to others by their mere proximity. The carriers were guilty of no criminal act, but were nevertheless incarcerated for life because of the constant danger they represented to others. From the point of view of social utility, such incarceration was surely justified; but Rothbard, not being a utilitarian, would not accept such justification. Yet from the point of view of criminal desert, there was no guilt at all, no guilty act which would constitute a just basis for such incarceration.

To Be Taken on Faith

In general, Rothbard's conten-

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tions on the many matters he discusses will seem most plausible to those who already have some knowledge of free-market economics. His statement of libertarian axioms and the consequences thereof will not be likely to carry conviction by themselves. Two examples must suffice:

(1) If you had reason to believe that Rothbard's views about ownership of land would have as a consequence that most land-ownership would become concentrated in the hands of a few owners, with the mass of people working for the owners, you might be less ready to accept Rothbard's views on the acquisition and transmission of property rights. You would be most likely to go along with his view if you had already been convinced, through *empirical* considerations (such as history), that such a result would not occur. (For example, it was Gabriel Kolko's *Triumph of Conservatism* that convinced me that ownership without government regulation would result in the dispersal of ownership rather than its centralization in the hands of a few.)

(2) If you believed that laissez faire would make a considerable portion of the population poorer even though it made some richer, you might well think twice about the acceptability of laissez faire: only after you had been shown by historical evidence that "a rising tide raises all boats" would you be inclined to accept it. A philosophy in which liberty was the paramount value (as in Rothbard) alone would not do it: "What good is liberty to a man if he's starving?" you might say. You would first have to be convinced that under laissez faire fewer people (or none) would starve than in any other economic system; only then would you be ready to accept the system. Doctrines of natural rights and property ownership alone would not do it.

In Quest of Justice

Even so, many persons will not follow Rothbard all the way in the way he traces out his philosophy of liberty. In Rothbard, for example, a person should not be coerced into doing anything as long as he has not treated others coercively. He is quite consistent with this principle when he alleges that no one should be forced to do jury duty or appear as a witness at someone's trial, even if his testimony would save the defendant's life. There should be no power of subpoena, for subpoena means coercion of the innocent. Even the defendant need not appear at his own trial. Rothbard is certainly consistent with his own stated principles here, and does not shrink from their consequences. Nevertheless the consequences might be such as to lead one to re-think or qualify the principles. Many persons, including many of Rothbard's fellow libertarians, are convinced that the most important

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factor in the case is the determination of guilt or innocence of the defendant—and that if a witness would be inconvenienced by appearing, he should nevertheless be required to appear, in the interests of justice.

Any voluntary exchange of goods or services (even lethal drugs), should be permitted, says Rothbard. If a blackmailer says to you, "I'll tell everyone your best-kept secrets, and thus cause you to lose your job and so on, unless you give me $10,000," this, says Rothbard, is a voluntary exchange, agreed to by both parties, and should not be prohibited.

What Is Voluntary?

In all this I fear that not enough attention has been given to the meaning of the term "voluntary." The fact that both parties agree to it is not enough to make it a voluntary transaction. For one thing, (1) coercion may be involved in the agreement, and when it is coerced it is not voluntary. Rothbard grants the coercion in the case of a robber who holds you up at gunpoint and says "Your money or your life" (though even here you have a choice, however unpleasant); he does not grant that coercion exists in the case of the blackmailer.

But there are other things besides coercion that can make an "agreement" less than voluntary, such as (2) extreme forms of psychological pressure. If a man is starving and he is told to sign a contract for labor for the next ten years at 10¢ an hour in return for a crust of bread now, and he agrees, is the agreement voluntary? If there is widespread unemployment and the only way a man can keep his job (there being no others in the area which he can obtain) is by agreeing to a homosexual tryst with the boss, is that agreement voluntary?

I would add that (3) having *knowledge* relevant to the case is also necessary: if the physician says to the prisoners "You'll all get out early if you let yourselves be inoculated with this vaccine," but doesn't tell them that the vaccine will have enduring painful side-effects and may even kill them, is their agreement to the experiment voluntary? Any presentation of a philosophy of voluntarism, such as Rothbard's, must be extremely careful to state the conditions under which an agreement, though assented to, is *not* voluntary. I would contend that the prisoners' agreement is not voluntary, since (as in cases of fraud) they would not have consented *if* they had known the full facts of the case.

Just as Rothbard oversimplifies the concept of voluntariness by considering any arrangement voluntary if it is agreed to by both parties, so he oversimplifies (in my opinion) the concept of *freedom* by saying that a person is free as long as he is not coerced by others. (He is surely right,

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however, in taking Hayek to task for mixing up the concept of coercion with other ingredients.) One is welcome, of course, to use the word "freedom" to mean simply absence of coercion, but it is worth pointing out that in our actual discourse we regularly use the terms "free," "freedom," and "liberty" to include much more than this.

> . . . the most general meaning of "freedom" is *lack of constraint* upon one's actions, and many things besides coercion can constrain.

I suggest that the most general meaning of "freedom" is *lack of constraint* upon one's actions, and many things besides coercion can constrain: coercion is only one (rather extreme) case. If a man is a compulsive gambler and through psychotherapy is rid of this tendency, he may quite rightly say that he is now free from his addiction, although no one was coercing him. (There are countless such cases of what psychologists call "internal compulsion.") If a woman obtains a divorce from her husband, she can now say that she is freed from her marriage bonds. Moreover, we are not only free *from* constraints of various kinds (negative freedom), we are also free *to* do certain things (positive freedom). The two are closely related: if I am free *from* the chains that bound me, I am free *to* walk about as I please. What others have called positive freedom, however, Rothbard does not call freedom at all.

If a man is starving on a desert island, Rothbard would say that he is free because no one is coercing him; if a mountain climber has fallen into a crevasse, and has no option but to wait for help to arrive, Rothbard would say the same, although there is clearly a difference between this man and one who is able to walk about, a difference which most of us would describe as the difference between being free and not being free—that is, free *to* do things which the unfree person cannot. As we constantly use the word "free," freedom does have something to do with the availability of *options* open to us—in general, the more options, the freer we are—although this very major ingredient of our ordinary concept of freedom is entirely excluded by Rothbard when he defines freedom in such a way as to cut all this off.

Utilitarianism Challenged

Throughout his treatment of these issues, Rothbard attacks utilitarianism. In my opinion he is justified in doing so—utilitarianism would, for example, condemn an innocent person to death if thereby some great social good (such as great happiness for others) could be realized. But this does not justify him in occasionally

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mischaracterizing the theory he is opposing. In Rothbard's example of the government officials who dissolve their government but as their last official act distribute all property rights in the nation to the Rockefellers and Kennedys of the realm, he says that this distribution would have to be accepted by utilitarians as a de facto accomplishment. But it would not. Nor would the utilitarian view necessarily be the one Rothbard attributes to it in the other example he cites.

Utilitarians are committed to only one thing, that the sum of the consequences of one's acts be the best possible when viewed in their totality—and the best consequences might well occur not from recognizing such claims but by denying them. In each case, one would have to examine each possible alternative and see which one was likely to result in the maximum amount of happiness (or well-being, or want-satisfaction, or whatever state is held by the individual utilitarian to be intrinsically good). It is not even necessarily true according to utilitarianism that it would be better to save two lives rather than one: if greater total happiness would result from saving the one (e.g., if he were an Einstein, or if the two had a predominance of misery in their lives), then the one should be saved: all that is required is that the greatest possible intrinsic good be achieved by one's action.

Even Bentham's stock formula "the greatest good of the greatest number" is inaccurate, for it sounds as if the happiness of the greatest number is to be preserved at the expense of the smaller number, whereas in fact *everyone* is to count in the total, the smaller number never being *ignored* but often being *outweighed.* Indeed, the wishes of a minority should (according to utilitarianism) sometimes prevail, e.g., if the granting of their wishes produced in the long run a higher total of happiness (including, of course, less unhappiness) than the granting of the wishes of the majority.

The Need for a State

There are policemen to enforce the law, and judges to interpret it. It would seem that there must also be legislatures whose function is to *make* the law. And doesn't all this require a government, a State? The State must be limited to a few essential functions, but isn't it necessary that a State, however limited, exist?

No, says Rothbard. Part 3 of his book is devoted to the extirpation of the State, root and branch. If to coerce people is to violate their rights, then the State as the No. 1 coercer of people must be eradicated totally. The State is incompatible with liberty, because it (1) coerces individuals into conformity with its laws, whether or not they wish to obey (and even if they find certain laws stupid or im-

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moral), and it also (2) pays for its activities through the power to tax, that is, to take money earned by individuals without those individuals' consent, which is theft.

How then are the rights of individuals to be protected without the State? Individuals voluntarily band together for their mutual protection into "defense agencies," in which other individuals are hired to protect their lives and property. These agencies are associated with "arbitration agencies," to decide the guilt or innocence of accused aggressors. The entire process of protection of rights could, according to Rothbard, proceed without the State, and much more justly and efficiently.

Anarchy vs. Law

These contentions open up once again the long-standing dispute among libertarian theorists between anarchy and limited government. The main arguments and counterarguments have been bandied about for so long that it would be tiresome to repeat them all here. (See, for example, Rothbard, *For a New Liberty,* vs. John Hospers, *Libertarianism.)* Given that an individual has a right to protect his person and property against aggression, it is quite a different question by what *means* he can best do this — this would seem to be a matter of strategy rather than of principle. It is true that the State currently does this through its power to tax, which is coercive. Some would say that for such necessary purposes a degree of coercion is justifiable; others would try to work out (as some have) methods of voluntary contribution to substitute for compulsory taxation. Whichever solution is adopted, several considerations could be advanced for preferring a single power, such as the State, to a set of competing agencies hired by individuals. I shall briefly summarize only a few of them here.

Chaos and Conflict

1. To have competing agencies working in the same geographical area would lead to chaos and conflict the moment they attempt to enforce different *rules.* And it seems to me virtually certain that this is what they would do. Different people have different ideals, and some of these ideals are held so strongly that their proponents would gladly use force to inflict them on others. This may be unfortunate, but as a feature of human beings it seems to me quite ineradicable. In the Bible belt, many persons (perhaps the majority) would gladly pay dues to agencies to enforce the closing down of X-rated movies and "adult bookstores," perhaps even arresting people for committing adultery or failing to believe in the literal inspiration of Scripture. Others would form an agency to protect themselves against

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all those who in their opinion constituted threats to "the morality of the community" or "those moral rules which keep together the fabric of society." Indeed, a group of murderers might form an agency "Murder Inc." and go about killing and looting. (I have never been convinced by arguments that such agencies would not come into being, or even in some circumstances prosper.)

As long as different people have different convictions and hold them strongly enough to be willing to use force to make others share them—and the lessons of history show us quite clearly that they would—we would have, instead of true "defense agencies," competing vigilante groups, the strongest of which in a given locality would force their edicts upon everyone as law. It is true that libertarians would "live and let live" except for aggressors against persons or property, but society is not composed exclusively of libertarians, and as long as this is so (and there is every evidence that it will continue to be so in the foreseeable future), the prospect of different agencies enforcing different rules must be squarely faced. Not only would different agencies *enforce* different edicts, they would *make* them, in the response to the (often whimsical, often evil) demands of their paying clients.

Rothbard alleges that once you have a government, no matter how limited, it will almost inevitably exceed its original powers (since it has the force to do so) and interfere coercively with people's lives. I agree: the tendency of limited governments is to become unlimited; that is why eternal vigilance is the price of liberty. But I am no more optimistic about the tendency of competing vigilante groups. Having the guns to defend you, they can use those same guns to attack you, and indeed to attack also nonmembers of their association who may be too weak to resist. What would prevent such an agency, or an alliance of such agencies, from ceasing to defend you, if they can get their spoils by force without having to render you the services which they have contracted to deliver?

. . . the tendency of limited governments is to become unlimited; that is why eternal vigilance is the price of liberty.

Advantages of One Agency

2. Quite aside from all this, there are distinct advantages in obtaining protection from a single political unit that protects persons and property throughout its domain. Suppose that Smith has minerals on his land worth $10 million, and that his neighbor, Jones, knows this. It will be worth

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at least $9 million to Jones to use his hired agency to take over Smith's land; and it would be worth at least $9 million for Smith to protect his land against such invasion. Such an expenditure would clearly be a waste of money for both parties. Would it not be preferable for both to have one agency, say the State, to protect each person's property rights? Both parties, knowing that the State would come to the aid of anyone whose rights were being violated, would usually refrain from violating them. Similarly, if you owned land along the Mexican border, you would have to spend so much of your income protecting it against trespassers that the price would probably exceed the income you could get from the land. No defense agency and no insurance company would be likely to take on such an expensive defensive operation, except at enormous cost; but a government would.

There are certainly cases in which individuals would have been wiped out by gangs of marauders superior in numbers, and have been rescued from this fate by government troops. Would Rothbard approve the presence of such troops (for defensive purposes only), in spite of his opposition to governments? Presumably not.

As Richard Taylor points out in his *Freedom, Anarchy, and the Law,* the State does not engage only in *prohibitory* activities (prohibiting certain kinds of actions), it also engages in what he calls *enabling* activities. By having the legal boundaries to your yard duly recorded in City Hall, you are enabled to call this property your own. You could indeed have a private agency record your ownership somewhere, but another claimant to your property could have the same piece of land recorded in *his* name at the offices of *his* agency. Who would actually take possession of the property would then depend on which agency had the most guns to defend its claim.

Similarly, if you wanted to adopt children you could go around bringing in homeless children, but unless there were *one* agency (e.g., the State) officially empowered to call them yours, what would prevent another person's agency from taking those same children from you a week later on behalf of one of his clients who would then call the children his? (An arbitration agency would settle the matter, it is said. But which arbitration agency would win out? In the end, the one with fewer guns would have to submit to the decision of the one with the most. Through the entire arbitration process both sides would know which one was stronger. Force, not justice, would become the ultimate arbiter of the dispute.)

Degrees of Evil in Government

3. Rothbard is opposed to all kinds of gradualism in getting rid of the

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State. If he could do so by pressing a button, he would abolish governments at once. But there are problems about this also, similar to the problems of removing life-support systems from very ill patients. If social security and welfare were stopped at once, with no period of interim adjustment, many thousands of people would probably starve. No police force would suffice to handle the looting and killing. With no system of voluntary financial help yet in place—not to mention the fact that Social Security recipients have been forced to pay into the fund, and thus have a justified claim on the return of their money—would Rothbard push a button that caused this to happen?

Would Rothbard not prefer the survival of a limited government to that of a totalitarian government? or would he say "a pox on both your houses" because they are both governments?

Surely there are at least *degrees* of evil in governments. Would Rothbard not prefer the survival of a limited government to that of a totalitarian government? or would he say "a pox on both your houses" because they are both governments? Would he have been against the American Revolution because its outcome was after all a government, even though it was a much more benevolent one, and more dedicated to individual rights, than any that had theretofore existed?

International Relations

All these problems are multiplied when we come to the matter of international relations. Rothbard's position is simple: there should be no political units called nations, hence *a fortiori* no relations among them. This, however, leaves numerous questions unanswered concerning the present world in which nations conspicuously do exist.

1. There are numerous problems involving national defense. At the moment these are handled by governments via taxation, and there is no foreseeable time in the future when this arrangement is likely to change. Will Rothbard tolerate national defense, at least *pro tem,* if the alternative is no defense at all? Suppose that (1) a nation stronger than ours attacks us, and that (2) no system of private voluntary defense is yet in place. Should the attack be countered with tax-supported defense forces, when the only alternative is annihilation? Surely to ask this question is already to answer it—unless the libertarian theorist is prepared to accept annihilation not only for himself but for everyone else, in the interests of his theory.

Libertarians, however, have con-

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. . . even if it were true that there is no external threat to Americans, it would not answer the question, "What should be done if there were?"

sistently downplayed this problem by alleging that there *is* in fact no real threat to the United States, and that therefore the problem does not arise. (But what about smaller, less powerful countries?) They have habitually distorted the data and played fast and loose with the facts in order to hold on to this answer. But the ploy cannot work: even if it were true that there is no external threat to Americans, it would not answer the question, "What should be done if there were?"

If the United States disbanded its armed forces today in the interests of libertarian theory, it would surely be ripe for the plucking by any aggressive nation that saw its chance to defeat us before any voluntary system of national defense could be established (if it ever could). If denationalization is to work, every nation would have to do it simultaneously. The chances of this happening are so infinitesimal as hardly to be worth discussing. (Besides, there is a whole array of problems concerning voluntary defense systems, such as the problem of freeloaders: enemy missiles will destroy the person and property of payers and nonpayers alike, so there is no obvious advantage, as there is in fire insurance on one's house, in paying one's dues to the "national defense" agency.)

The fact seems to me quite clear: survival is not merely optional. In the 1930s most Western nations apparently believed that if they reduced their defense forces, Hitler would do the same. More than 50 million deaths in World War II resulted from this mistake. The same mistake was made in the 1970s, of which we may yet reap similar consequences. Only a strong deterrence stands between us and destruction. To say that there should be no deterrence because it is after all undertaken by that greatest of evils, namely nations, is to blind oneself to an even greater evil, namely annihilation.

Multiple National Defenders

2. If, for a single national defense, one substitutes a series of competing agencies to which people pay dues to defend themselves against external attack, other problems arise. Defense agency A may decide that nation X is the greatest potential threat, and agency B that nation Y is the principal threat—and their strategies will differ accordingly. Even if both agree that nation X is the enemy, the *means* of defending ourselves against X may well be a matter for disagreement: the strat-

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egies of various agencies might even get in each other's way, and the entire attempt at defense might prove ineffectual as a result. There is surely an advantage in having *one* defense policy rather than a multiplicity of them whose total effect might be chaos. Competition in laundry soaps is healthy and productive; competition in defense strategies, with each one being implemented by a percentage of the population, could well prove disastrous. There are some things that it's better to have just *one* of, and it may be that official records of property ownership and unified defense strategies are among them.

An Indefensible Position

3. There is an additional problem as well. Rothbard claims that the only justified war is one that does not involve even *one* person who wants no part of it. These are indeed heroic words, and a consistent application of his own principles. But suppose now that a totalitarian nation attacks us, and that the only way to protect ourselves is through a massive defense system (not retaliating by aiming our missiles at the aggressor, but simply neutralizing the aggressor's missiles against us). Suppose, however, that as a result of undertaking this defense, just *one* person who wanted no part of it was inadvertently killed. Would Rothbard hold that therefore no such defense should be undertaken? Apparently he would. But what if the alternative to undertaking such defense is that *many* people would be killed in the enemy attack?

Would Rothbard say that the American Revolution should not have been undertaken, even though it was to a large extent a libertarian revolution, if in the course of its occurrence just one person who didn't want to take sides in the struggle was killed or maimed? No one, of course, wants to sanction the death of even one innocent person; but what if the only alternative, in the real world rather than that of libertarian theory, is the death of many more?

Like Tolstoy in *What Is Art?*, Rothbard does not shrink from the consequences of his own principles; indeed, he traces them confidently and proudly. But some of these consequences are so controversial, and some others so downright alarming, that, while accepting that they *are* consequences of the principles initially laid down, many readers will prefer to re-examine the principles themselves, and attempt to qualify them in such a way as not to yield the "wildest" and most "far-out" of the consequences.

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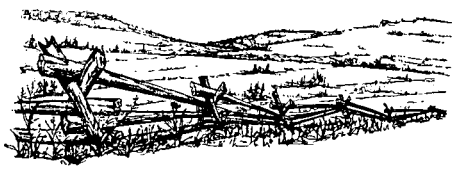
Glenn L. Pearson

Mixed Economies A No-Man's Land



In a recent address at a local university, a popular liberal explained that America had been forced to turn to a mixed economy because of the "excesses of free enterprise." These excesses, he explained, were caused by a lack of social conscience, evidenced by high profits.

He quite rightly defined our mixed economy as a combination of welfare statism, Keynesian money policies and rigorous business controls bureaucratically enforced on the remnants and tatters of a market economy—though he didn't call them remnants and tatters. His description of what is left of the so-called private business community sounded more like a dinosaur with little brains, no conscience and an insatiable appetite behind mass and muscle that will never run out no matter how much it is controlled or starved.

This professor told his audience that our mixed economy is adequately productive and more just and equitable than the free market was or would be now if we still had it. But he left out a series of facts that the typical university audience would not see, such as the following:

1. The introduction of a mixed economy was a declaration of war against freedom and property. "A mixed economy" is a euphemism for this state of war. It implies—as did this professor—that free enterprise and socialism can exist together peaceably, that by some kind of social compact this lamb can be caged with this lion and we will wake up morning after morning and find both animals purring and bleating happily together. In order to introduce any aspect of socialism the individual's right to own and control property has to be breached. It must be legal for the government (that is,

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elected or appointed people) to seize private property and use it for some purpose that favors one class or person over another. The government (that is, people with power) has to have this right to seize property for purposes that do not in theory or practice benefit all equally, and has to have the discretionary privilege of determining just which persons will be benefited at the expense of the rest of us.

When this power has been granted, a potential for total socialism exists. That is, once we give the government (that is, people) the power to tax for any purpose but justice and defense, we have unlocked the door to total socialism. It is only a matter of time until, in the discretion we have granted them, *people* in government will choose to go all the way. There really isn't any way we can give these politicians and bureaucrats (we impersonalize them by calling them "government") a fraction of this power to redistribute private property. We gave them all of this power when we thought we gave them some of it. The past several decades are a well-documented history of this fact.

2. People, not economies, are controlled. Any economic policy imposed by law or administered by bureaucrats has all its effect on people. Remove all the people and what would be left? Would it do anything? Go on producing? Perpetuate itself? Of course not. Plants and sub-human animals would take over and struggle for survival in a world that would know nothing of economies, free or controlled.

The possibility of economic upward mobility was the condition that brought millions of immigrants to America. We cannot have economic upward mobility for long in a mixed economy, and not at all in socialism. The poor need property rights more than anyone else.

We should not pass a law that we would not wish to affect us as we wish it to affect someone else. That is not just a restatement of the Golden Rule. It is a matter of practical application: we could be there and be affected by that wicked and unjust law that we wanted only for reasons of envy in the first place.

We should never endow a political office with powers we would not want a wicked person to exercise; because, sooner or later, that wicked person will be in that office even if only temporarily. Wicked people are more prone to seek office than are good people. And the more power and discretion we put in an office the more actively and vigorously will wicked people seek it.

3. People are mixed, not economies. That is, in what we call a mixed economy, what we have is a mixture of two classes of people—those who

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are in the socialist side and those who are in the non-socialist side. And they have different ends and different means of reaching them. These two classes are at war with each other. Sometimes the bureaucrats are at war internally with themselves. While at work, they have to do things that are acts of war against themselves in their private lives. A mixed economy is a schizoid state of affairs that promotes no end of warfare and turmoil in souls and in society. It is a no-man's land. Imagine the torture to a Christian, for example, who tries to keep any significant meaning for the Ten Commandments and the Sermon on The Mount and still pretends to see justice and equity in socialism.

4. Human nature isn't changed by a change of social or economic orders. It can be improved by such things as persuasion and example; but people are not better or worse in a mixed economy or in a free economy except as the opportunity or incentive to sin is increased or decreased. The law is simply a standard that determines what is good or evil for ethical purposes in people of good conscience and for legal purposes in the judgment and punishment of criminals.

If the law is perverted or unjust, it will destroy respect and increase crime. It will do this even if the perversion and injustice are not perceived on a conscious level. The subconscious also can sense perversion and recoil at injustice. It may well be that the violation of conscience that is not dealt with openly does more harm and explains more violence than do problems that are perceived and dealt with rationally. That socialism which is found in a mixed economy is especially offensive to people of fine and noble sensitivities because it is so blatantly unjust to say that, by hiring a person as a government employee, we can authorize and sanctify all sorts of deeds of routine violence to property rights that a person cannot perform in the role of private citizen without indictment as a criminal.

5. In many ways mixed economies increase the incentive and opportunity to commit crimes. In a free society those rich who are selfish can only misuse their own money. In a mixed economy, there is a great incentive for all kinds of criminals to get control of the government so they can use both money and power to achieve evil ends. The more bureaucratic positions available, the greater chance of criminals holding office; and this facilitates the growth of all sorts of bribery. It also opens the door to employment padding, nepotism, misuse of privileges (like franking mail and making long distance calls on WATS lines) and all sorts of graft. Some of this graft is now so much a

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way of life that we just live with it.

Many of those "awful, wicked, unconscionable" free enterprisers are now awful, wicked unconscionable bureaucrats. In fact, it may well be that the more incompetent and prone to evil they are, the more likely they will be to gravitate out of the risk, competition and governmental intervention of business and into the security of government. Of course, not all bureaucrats—maybe not even most—are fearful, sneaky, lazy and prone to graft and bribery; but certianly such people are far more at home in government than out in the rigorous world of business. Else why the periodic and extensive purges in Russia and China?

In very recent times the Chinese Communists have declared the presence in their extensive bureaucracy of all the evils listed above, and they have tried to purge them out.[1] But, again, they can only purge people and replace them with people. It is a law of bureaucracy that the most evil men are the best at appearing good. Another bureaucratic law is that power corrupts most people. So, even if we replace bad bureaucrats with good ones, many of the good ones will get bad by and by. Enough will get bad so that purges improve bureaucracies only temporarily.

6. The free market is not devious about profit. Without profit there is no reason to stay in business. That is an honest, up-front fact. But consider this: the socialist sector in a mixed economy (TVA, public roads, postal system, public schools, and so on) have a substitute for profit: taxes. They tax for all the reasons business seeks profit: large salaries and benefits for management, plant expansion, modernization, research, and the like. And taxes are not controlled by the natural laws of the market place.

7. Capital is the basis of production in all economies. It can be created only by savings. Someone has to cut down on consumption and divert savings to machinery, land and operating capital. Once capital has been created, it can be obtained by borrowing. It also can be obtained by stealing it. In that case, there isn't any overall increase of capital likely to ensue. It is just transferred from one person or segment of society to another. That is why the socialism we have in our mixed economy is such a burden—it steals (gets by taxation) all of its capital from the business sector. Then, to add insult to injury, the socialists accuse business of inefficiency and lack of social conscience for seeking a profit that

[1]See, for example, "Corruption, Scandals Prompt Chinese to Clean Up, Reform Party," by Victoria Graham, Associated Press Writer, *The Salt Lake Tribune,* Sunday, October 11, 1981, p. 12A.

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can rebuild its capital. When they occasionally see that their taxing policies have prostrated business, they introduce tax reforms temporarily to help business get back on its feet. Each time the tax laws are changed, they get more confused and complex.

The so-called Third World is full of nations that are experimenting with socialism of various mixtures. They look with envy upon the capital of the American Business community and that of any other country which has had sufficiently free economies to accumulate capital. The United States government quite regularly accommodates that envy by plundering our business community to start or perpetuate these socialist experiments. Conceivably, for short periods, a socialist country might accumulate capital at great sacrifice and hardship to its citizens. But too much of the accumulation of capital in the slave world is being accomplished at the expense of whatever business in the "free world" there is left to tax. In the long run, of course, socialism will not work.

8. Justice and equity are ideals that are never fully achieved. However, they can be approximated in a market economy because the government in that case is not in the business of injustice. In a mixed economy, all that the government does to redistribute wealth is, by definition, injustice; because it is designed to discriminate. In a market economy the government is confined to the task of protection from criminals and foreign aggression. The president is the high sheriff and commander-in-chief. He has no proposals to improve the economy or bring relief to the poor and unfortunate unless that relief is a matter of national or local defense that is clearly constitutional. And the more we attempt to change that state of affairs, the more we introduce injustice and inequity into society. We show an unfortunate misunderstanding of definitions when we equate justice with economic equality.

9. There is reason to doubt that the establishment of a mixed economy was motivated only by misguided concern for the poor and afflicted. This doubt is fed by at least three historical facts. The first of these facts is that the prime-movers—especially those who were intellectuals and labor leaders (such as Thorstein Veblen, John Dewey, Eugene Debs, and the like)—who were most effective in pushing us into a mixed economy were Marxists of some stripe or another, whether or not they were members of a Marxist society. The mixed economy usually was not and is not a goal, but only a signpost on a much longer road.

The second historical fact that casts

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a shadow on the motives of those who pushed us into a mixed economy is that the poor have increased as the mixing of the economy has increased. The number who perceive themselves as poor has increased dramatically. This is because the welfare state philosophy feeds envy. The number who are perceived as poor by those who administer state relief has increased dramatically. This is because there is personal advantage and gain for these bureaucrats if their relief programs grow. But those who are objectively poor, in the life and health threatening sense, have increased also. This is because a mixed economy cuts off avenues of upward mobility and tends to throttle private concern for the poor.

The third historical fact is that bureaucracies are run for the good and the perpetuation of the bureaucracies, not for the help of those they ostensibly were set up to serve. Ludwig von Mises and many others have adequately proved this both rationally and empirically. Consider this one fact: if you divide the amount of tax revenue budgeted to the bureaucracies for the care of the poor by the number of poor these bureaucrats say we have, there is no way you can come up with less than $6,000 per person per year in 1982 dollars. Some studies have put the figure much higher. It is difficult to pinpoint a correct numerator or denominator because so much public charity is hidden in so many different places—housing, food stamps, medical care, subsidies, student loans, and so on.

The breakdown of the federal budget sent out in March, 1982 by Representative Dan Marriott of Utah shows categories that are mixed in such a way that it is impossible to determine the dollar amounts meant for the poor. Nevertheless, the sums earmarked for a number of agencies and programs that were originally set up to relieve poverty and distress totals at least 577.6 billion dollars. However, an unknown amount of billions in this 577.6 billion is now meant for others than the truly poor and distressed; but nearly all of it is justified to the American taxpayers as absolutely necessary relief from some kind of hardship suffered by somebody.

Just as a practical illustration, suppose you accept 34 million as the number who are so poor as to truly need immediate and continuing aid. Suppose you gave each one—men, women and children—$6,000 annually. (That would be $24,000 per year for a family of four. No end of families of six to ten in Utah and, no doubt, elsewhere, are doing very well on that much without public relief other than such indirect programs as FHA home loans. These families also are contributing ten to fifteen per cent of their income to private care of the poor or to other charita-

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ble causes.) Now multiply $6,000 times 34 million and you will get a product of $204 billion. That is only 35% of the $577.6 billion we started with. Remember, also, that every state is in the welfare business. Then you will see that $6,000 per year per person would leave a great deal for necessary administration.

And the truly poor don't get anywhere near $6,000 per year. Where, then, does the money go? Most of it goes to the care and keeping of the bureaucracy, which, in turn, helps perpetuate in office the kind of people who will keep the budget rolling in to perpetuate and expand the bureaucracies. This is the sort of thing that creates doubt about the sincerity of those who say the poor need a mixed economy to save them from the wicked free enterprisers. One cannot help suspecting that the money is going just exactly where it was meant to go by those who got us into this mess.

10. The rich can get richer while the poor are getting poorer in a socialist economy; because those with the power (the bureaucrats or ruling class) can divert whatever wealth they want to themselves for whatever purposes they choose. In a free market economy, the rich cannot get richer at the expense of the poor. Inevitably they make the poor richer. Everything they do with their wealth creates opportunities for others. The only way they can prevent this from happening is not doing anything with their wealth—not consuming any of it, not investing any of it, just hoarding it. And who does that? Only the very few who are insane.

There is no legal way for a rich man to cause a poor man to get poorer while enriching himself in a market economy that is protected from criminals and foreign invaders by a government that is limited to defense by constitutional law. True, our original Constitution looked the other way at slavery, to put it charitably. That was a flaw that cost much more blood, both by the whip and by the sword, than was shed to prepare the way for the original document. So we must not forget that blood—and all the blood—that was shed to get us out of the very thing the socialists are working so hard to get us back into—slavery.

11. In a mixed economy, the socialists can blame all failures on the business community—and they do. They do not publish the fact that all the same economic and social problems exist in an even more aggravated state in countries that are nearly all socialist. The professor who inspired this article tacitly agreed that a market economy is successful when he said that there was too much profit in a market economy. Socialist countries never have *that* problem.

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Thomas J. DiLorenzo

Public Policy & The Free Economy

TAXPAYERS in the United States, Great Britain, and several other democratic countries have become increasingly disenchanted with the unfulfilled promises of governments, the burdens of taxation and inflation, and the loss of individual freedom which public sector expansion has generated. New constitutional and statutory restrictions on governmental taxing and spending powers have been imposed in the U.S. and both Ronald Reagan and Margaret Thatcher were elected on platforms which called for a relative reduction in the size and scope of government and the encouragement of free enterprise. But a dangerous scenario is being constructed in the U.S. and the U.K.

Entrenched government bureaucracies along with labor unions and other powerful interest groups have prohibited any significant reductions in government spending, and the basic government regulatory institutions which have placed such heavy burdens on the private economies of the U.S. and Great Britain remain largely intact. Left-leaning politicians now publicly express a desire for higher inflation and unemployment which they hope will help to restore their political power, and the media routinely reports, incorrectly, that both the Thatcher and Reagan economic platforms have been implemented, and have failed. The danger in this situation lies in the fact that it is customary to hold the chief executive responsible for the health of a nation's economy, regardless of what the causes of current economic problems might be.

The problems of inflation and unemployment, which are primarily caused by past government interventions in the market economy, are being widely sold as the direct result of policies which encourage free enterprise and attempt to restore incentives to work and invest. It is

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therefore of utmost importance to set the record straight, to clarify this issue, and to strengthen public support for the free economy. This paper attempts to make a contribution toward that end by discussing the virtues of the free economy. A major theme of the paper is that in the (free) market economy individuals, acting in their own self-interests, are induced by the spontaneous forces of the market to act in ways which serve to maximize social welfare; by contrast, it is shown how government control over the allocation of resources redirects the forces of rational self-interest in a way that allows elite groups within government to impose forcefully their will upon others, which in turn causes a reduction in wealth and in individual welfare.

The Sovereignty of the Consumer

In the market economy the production and distribution of goods and services is determined by the decisions of entrepreneurs, and this fact has generated much wrath on the part of many members of society, especially intellectuals, and especially those in the social sciences and the humanities. Entrepreneurs are often portrayed as being hard hearted and callous, and responsible to no one. But in the free economy they are not.

Economic affairs in the market economy may be *directed* by entrepreneurs, but *consumers* are the ultimate decision-makers. Consumers determine what is produced and, as Mises has said, it is they who ". . . in their capacity as buyers and consumers . . . are hard hearted and callous without consideration for other people."[1] That is, consumers patronize those who can offer the highest quality products for the lowest prices. Those who do not meet the demands of consumers will suffer losses or go bankrupt and will therefore be removed from their "positions of eminence," while those who cater to the desires of consumers will be rewarded with profits. Both the carrot of reward and the stick of punishment (for ignoring consumers' preferences) contribute to the success of the market economy.

Not only are entrepreneurs induced by the market to satisfy consumers' preferences for goods and services, but they are also motivated to provide goods and services at the least possible cost, for in a competitive economy those who fail to do so will not survive. Entrepreneurs who do not make the best use of available time, knowledge, and resources bear the risk of bankruptcy or, alternatively, of being replaced by "takeover raiders" via the market for corporate control. There always exist enterprising individuals who are willing to take over, through stock purchases, private enterprises that do not adequately meet the demands

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of consumers, for the substitution of more efficient for less efficient management promises the reward of higher profits. Those opposed to corporate takeovers would have us abolish the market for corporate control, but fail to acknowledge the damage such restrictions would inflict upon the consumer. Arguments against the market for corporate control thus appear to be nothing other than disguised protectionism.

How the Market Functions

In the market economy the consumer determines not only the pattern of prices and production, but also the distribution of income. That is, the consumer ultimately pays the wages of all workers, whether they be professional athletes or street vendors. The greater the consumer demand for a good or service, the more an employer will be willing to pay the worker who can produce the product, as long as labor markets are competitive.

The employer who pays his employees less than their marginal contribution to the firm's profits will not do well and may very well fail. The baseball team owner, for example, who pays gifted, star athletes the salary of a college professor will most likely bear the burden of a poor record and consequently, lower profits. The same can be said for the management of steel mills, textile plants, grocery stores and all other private enterprises. Thus, in a free economy one's income depends upon one's ability to satisfy consumers. It is in this way that the spontaneous forces of the market serve to maximize individual welfare.

The Hazards of Consumer Protectionism

The virtues of the free economy are amplified once they're compared directly to the vices of interventionism, and an appropriate starting point is the example of "consumer protection regulation" which is quite prevalent in the U.S. and exists in most other industrialized democratic countries as well.

The federal government is intimately involved in the regulation of trade in the U.S., and has been ever since such muckrakers as Upton Sinclair (author of *The Jungle*), Ralph Nader, and Senator Estes Kefauver (whose investigations of the drug industry led to the expanded powers of the Food and Drug Administration) began attacking the quality of products manufactured by private producers. Self-appointed "protectors" of the consumer now staff hundreds of government agencies, and under the guise of consumer protection perform tasks which unequivocally make the consumer *worse* off, as can be illustrated by the example of the Consumer Product Safety Commission, which serves as a prototype for scores

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of other "consumer protection agencies."

The Commission is mandated to perform a task it cannot possibly achieve — "to protect the public against unreasonable risks of injury from consumer products. . ." Its authority covers "any article produced or distributed except for certain items already regulated by other government agencies." The objective of safer products is desirable, but the important question is: At what cost and by whose standards? A safer automobile which is slower, heavier, and more expensive than others may have some advantages, but how can a government bureaucrat possibly know how much safety individual consumers are willing to trade off for speed and lower prices? Besides, it is not clear that "safer" vehicles cause fewer accidents. It may be true that safer vehicles induce carelessness by drivers which leads to *more* accidents which are mainly caused, after all, by human error. The governmental banning of various "dangerous" products deprives the consumer the right to make the relevant tradeoffs, which only he can make, and therefore reduces his welfare.

A rather blatant example of how the "consumer protectionist mentality" has gone to extremes is the appearance of the recently dethroned director of the National Highway Transportation Safety Administration on a popular television program. The ex-director was accompanied by a masked man with a sledge hammer and an automobile produced by a private engineering firm, employed by the government, which was allegedly crash-proof. After observing the masked man fail to dent the automobile with the sledge hammer, the ex-director opined how wonderful it would be if the government were to require all automobiles to be just as sturdy. When pressed by a member of the audience, the ex-director reluctantly stated that the cost of such a car is approximately $200,000 — hardly a price which would "protect" the consumer. Only freedom of choice, and only a free market economy is capable of accomplishing that task. So-called consumer protectionism is merely a way of forcefully substituting the will of a few non-elected government bureaucrats for that of the general public.

Product Information and the Free Economy

There are many who claim that private advertising is misleading, and induces consumers to purchase things they would not otherwise purchase. Therefore, so it is claimed, advertising should be controlled or regulated by government, if not abolished, in order to avoid "consumer exploitation." But how can a consumer be exploited if he *voluntarily* purchases one brand of say,

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toothpaste over another? As long as advertising is competitive, and the consumer is free to compare and contrast the competing claims of advertisers, it is impossible for him to be "exploited." In fact, quite the opposite is true.

It is the *absence* of advertising which is detrimental to the consumer, since one of the major reasons for advertising is to publicize price and product quality. Take, for example, the case of law firms in the U.S. which until recently were banned from advertising. Such a ban on advertising is nothing more than special interest legislation which benefited existing, established law firms at the time the legislation was put into effect, to the detriment of newer firms and consumers. The older, established firms had little need to advertise the price and quality of their product, for their reputations had already been established, and the most prominent members of the legal profession are much sought after by these firms not only for their skills, but also for the right to place their names on the firm's letterhead to send out the desired market signal.

Newer, less established firms who must compete with the more experienced firms must do so by offering a "quality" product at a competitive (lower) price. The ability to advertise lower prices is one way to induce consumers to make use of their services. After all, many consumers would prefer not to have "Cadillac quality" legal services at Cadillac prices, but would prefer a wider range of choice. Bans on advertising preclude the consumer from making any such choices and therefore allow the established firms to charge higher prices than otherwise.

As another contemporary example, it is difficult to believe that one of the largest hotel/motel chains in America is actively lobbying against roadside advertising "for the purpose of enhancing the beauty of the environment" rather than a desire to stifle price competition from less well-known hotel chains.

In sum, the idea that consumers can be led by the nose by advertising has been proven false time and again. Regardless of how much Ford Motor Company advertises another "Edsel" automobile, it won't sell. As economist Harold Demsetz of UCLA has found, the profit maximizing firm will find it more sensible to first find out what consumers want, and then produce and advertise it. Surely, this would be more lucrative than spending millions trying to convince consumers to buy green wigs or lead tennis balls.

The Price System

As the Friedmans have said, the key insight to Adam Smith's *Wealth of Nations* is misleadingly simple and, unfortunately, widely misun-

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derstood: In a free market economy, voluntary exchange will not take place between two parties unless both believe they will benefit from it.[2] It is *not* true that one party can benefit only at the expense of another or that, in international trade, firms in one country benefit at the expense of those in another. Free trade is *mutually* advantageous. This insight is obvious when one considers trade between two individuals, but it is more difficult to understand how people living all over the world can cooperate to promote their own interests. It is the price system which accomplishes this task in a market economy, without any need for central direction of prices or production by the coercive powers of the state. Thus, Adam Smith's crowning achievement was to recognize that the prices which emerge from the voluntary transactions between buyers and sellers in a free market could coordinate the activities of millions of people in a way in which everyone, acting in his own self-interest, is made better off.

Two major functions of the price system are to transmit information and to provide incentives to adopt least-cost methods of production. Consider the effects of say, an increase in the consumer demand for bicycles. Retailers will find that they are selling more bicycles and that consumers are willing to pay more for them. They will therefore order more from wholesalers who in turn will order more from manufacturers. Manufacturers will order more steel, rubber, chrome, plastic, and all the other materials used to produce bicycles. In order to induce the suppliers of these inputs to produce more, manufacturers will have to offer higher prices. The higher prices induce input suppliers to employ more people to meet the increased demand. To do so will require that they offer higher wages or fringe benefits or better working conditions. Thus, in this way the price system transmits the message that there has been an increased demand for bicycles and that consumers now prefer the additional use of resources to produce them. There is no need for any one person or agency to "coordinate" any or all of the above activities. Such an effort would indeed be fruitless, since no one individual or group of computer programmers could possibly gather and use all of the relevant information.

Information Flows Both Ways

Prices not only transmit information from consumers to retailers, wholesalers, manufacturers and resource owners; they also do the opposite. For example, if for some reason imports of rubber into the U.S. were reduced or cut off, the reduced supply would increase the price of rubber and of all rubber products. It will not pay to produce as many bi-

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cycles as before. The smaller supply of bicycles will increase the price which will inform consumers to take better care of their bicycles and to keep them longer or to consider alternative forms of recreation.

Any governmental controls which prohibit prices from expressing changes in supply and demand conditions stifle the dissemination of important information. For example, price ceilings placed on oil and other fuels in the U.S. prohibited information about the effects of the OPEC cartel from being conveyed to producers and consumers. Price ceilings on oil artificially stimulated the demand for oil and gas and reduced supply, creating shortages which were compensated for by increasing imports even more. Because of price controls, the *real* price of gasoline actually *fell* from November 1973 to May 1979, which conveyed to consumers the message that gasoline had *not* become more scarce, and that it was not worthwhile to conserve more energy than previously. The automobile industry, in responding to the demands of American consumers, did not significantly increase production of smaller, more fuel-efficient cars.

Now that the real price of gasoline has risen since the controls have been lifted, the auto industry finds itself at a severe competitive disadvantage in international competition. American consumers were also forced, because of price controls, to finance through taxes the activities of a Department of Energy which spent about $10 billion in 1979, employed 20,000 people, and admits (optimistically) to having no positive effect on energy problems.

A further virtue of the market economy is that the price system provides producers with incentives to seek the most efficient means of production—those means which use the least resources, leaving more resources for other uses. For example, there are literally thousands of different types or grades of steel. When the supply of one type of steel is curtailed, which raises its price relative to others, producers of automobiles and other products will substitute the less costly types of steel. Reducing the cost of production enables the producer to increase the gap between revenues and costs. Any governmental controls over the prices of factors of production—via minimum wage laws, by trade unions, taxes, subsidies—distorts information transmitted by the price system and makes it impossible to discover least-cost production techniques.

Consumer Sovereignty vs. Politician's Sovereignty

In the market economy consumers are said to "vote with their dollars." Unlike the political market place, where one level of output is provided to all, producers provide different

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amounts of goods and services to consumers, depending on their income and preferences. Those who are willing and able to pay can consume all they want at the existing market prices and, as described above, the production and distribution of goods and services is dictated by the wishes of consumers.

There are many, of course, who are dissatisfied with the way in which the free market allocates resources. Among the most frequently cited objections are that the market generates "inequities," does not sufficiently protect "the poor," is based on greed (read the profit motive) rather than selflessness, and leads to shortsighted outcomes which lack long-range perspectives. As a result of these alleged problems, so the interventionists argue, there is a need for greater political control of the allocation of resources by those who are wise enough, selfless enough, farsighted enough, and sufficiently egalitarian to correct these problems. In short, according to this view, social problems are best dealt with by a delegation of benevolent and omniscient despots, if any can be found. This is a caricature of the conventional view of public policy in the U.S. and in many other democratic countries, and illustrates the dominant themes of the "public administration" literature from Confucius and Plato to Woodrow Wilson and their contemporaries.

Failures of Intervention

The miserable failures of governments to effectively deal with the problems of poverty, the low quality of primary and secondary education, energy, housing, and so on are usually explained in terms of the personal attributes of politicians and bureaucrats: They are evil or stupid, lack sufficient authority and funding, or lack sufficient information. The problems of social policy are then merely a matter of selecting sufficiently wise and benevolent despots and giving them power and knowledge. But the harsh lessons of recent history have shown that good men do not guarantee good government.

It is most unfortunate that much of the American public has become enchanted with the "Platonian" view of government intervention and seems to have forgotten the important principles upon which the federal constitution was based. Namely, the authors of the *Federalist Papers* were concerned with giving government enough power to carry out its responsibilities, but not so much power that the rights of individuals would be infringed. They held that one cannot control the excesses of government by merely electing the "right" people, as the following statement by James Madison illustrates.

> It is in vain to say that enlightened statesmen will be able to adjust these

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clashing interests and render them all subservient to the public good. Enlightened statesmen will not always be at the helm. . . We well know that neither moral nor religious motives can be relied on as an adequate control.[3]

Alexander Hamilton was also reluctant to rely on the innate goodness of man, for to do so

. . . would be to forget that men are ambitious, vindictive, and rapacious. . . Has it not, on the contrary, invariably been found that momentary passions, and immediate interests, have a more active and imperious control over human conduct than general or remote considerations of policy, utility, or justice?[4]

Because of these views, the framers of the Constitution were careful to adopt institutional arrangements which would constrain the coercive powers of government, for as Madison argued,

. . . what is government itself but the greatest of all reflections on human nature? If men were angels, no government would be necessary. If angels were to govern men, neither external nor internal controls on government would be necessary.[5]

In reflecting upon the secular growth of governmental powers in the U.S. a contemporary student of constitutional reform, James Buchanan, has further observed,

Politicians are politicians because they want to be. They are no more robots than other men. Yet the politician who would do nothing other than reflect the preferences of his constituents would, in fact, be robotlike in his behavior. Few, if any, politicians are so restricted. They seek office because they seek "profit," in the form of "political income," which will normally be obtained only if their behavior is not fully in accord with the desires of electoral majorities. Those men who are attracted to politics as a profession are likely to be precisely those who have considerable interest in promoting their own version of good government, along with those who see the opportunities for direct and indirect bribes, and those who evaluate political office as a means toward other ends.[6]

Political Control

Thus, it has long been recognized that when political resource allocation replaces the market allocation of resources, the results are not likely to be either equitable or efficient, unless by sheer accident. How resources are allocated depends largely on the different opportunities for "political profit" which alternative allocations present to the political decision-maker, for politicians, like all other human beings, act so as to pursue their own self-interests. Consumers' sovereignty is replaced by the sovereignty of the politician/bureaucrat, and the two often do not coincide. Consumer demand no longer determines the pattern of production and distribution. Instead, an individual or group's ability to receive goods and services depends not only on their ability to

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"compete with their dollars," but on other forms of competition as well, which are expressed through political power and influence, violence, and various forms of bureaucratic manipulation.

Political resource allocation, consequently, often entails effects which most would consider perverse and inequitable. As one example, consider the decision made by the U.S. Congress in 1949 to grant the government a greater role in the provision of housing by embarking on a program of "housing and urban renewal" which was aimed at providing benefits for the poor. In the early history of urban renewal the evidence clearly shows that more housing for the poor was demolished than was replaced. Between 1949 and 1963 the 106 completed urban renewal projects had demolished about twice as many units as were replaced, and only 8 percent of the replacement units were in public housing where "the poor" could gain access.[7] Evidently, middle and upper income groups are not only better able to vote with their dollars than are the poor, but are also more politically influential and have been major beneficiaries, along with government administrators, of the many urban renewal programs in the U.S. Similar outcomes have resulted from government interventions in the areas of energy, education, welfare, and so on.

The inequities which often stem from political resource allocation are made more clear when one observes resource allocation in nondemocratic, or socialist countries such as the Soviet Union where those in power, along with their families and friends, are at the top of the income scale, while in the name of "egalitarianism," nearly everyone else is put in his place at the bottom, and is kept there by threat of violence or imprisonment, as recent events in Poland illustrate.

Inequitable and Inefficient

When the market allocation of resources is replaced by political resource allocation the results are often inequitable *and* inefficient, in that more resources tend to be expended on activities which merely redistribute wealth rather than create wealth. Government, after all, does not produce much of anything; it takes from some and gives to others, keeping as much as it can for itself in the form of discretionary revenues.[8]

In democratic countries there is an asymmetry between the benefit incidence of political decisions and the tax incidence. That is, beneficiary groups or recipients of government-financed transfers tend to be concentrated, or organized, and capable of influencing politicians. By contrast, taxpayers tend to be widely dispersed, with little incentive to ac-

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tively oppose individual transfer programs. As a result of this asymmetry there is a structural bias toward expanded levels of government spending and taxing. As the government sector expands, more and more resources are used by all the various interest groups to lobby for transfers rather than to produce goods and services, which serves to diminish the total wealth of nations. As wealth transfers increase, the private sector, which is the sole source of wealth *creation,* is increasingly crowded out.

The Problem of Monopoly

The virtues of the market economy are partly undermined by the existence of monopoly power. A monopolist who, by definition, is the sole supplier of a product for which there are no close substitutes will restrict output, thereby raising his price above what would be paid if markets were competitive. Consumers are made worse off because some of their wealth is transferred to the monopolist, and because fewer resources are devoted to the production of the monopolized good (and more to other goods) than what consumers would prefer with freer trade.

Over the past several decades many have claimed that the allegedly increased concentration of industry in the U.S. and in other democratic countries has led to increased monopoly power and therefore calls for a greater degree of governmental control, regulation, or outright ownership of industry. Even though there is no evidence that American industry has become increasingly concentrated over the past century or that concentration *per se* leads to monopoly profits, such unfounded sentiments can be understood if one recognizes that it is the interventionists themselves who intend to become the regulators, the controllers, and the managers of nationalized industries.

The claims that government regulation of industry is a necessary condition for the *prevention* of monopoly power have ignored history and reality. Adam Smith himself was among the first to recognize that government regulation of industry is the sole *cause* of monopoly, not a remedy for its ill effects. Smith viewed the regulation of industry as a means of redistributing income to potential monopolists who would in turn provide political and economic support to the government. He observed that the various trades in eighteenth-century Britain which were *granted* a monopoly status gained such status because of a comparative advantage in lobbying.

> Country gentlemen and farmers, dispersed in different parts of the country, cannot so easily combine as merchants and manufacturers, who being collected into towns, and accustomed to that exclusive corporation spirit which prevails in them, naturally to endeavour to ob-

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tain against all their countrymen, the same exclusive privilege which they generally possess against the inhabitants of their respective towns. They accordingly seem to have been the original inventors of those restraints upon the importation of foreign goods, which secure to them the monopoly of the home market.[9]

Smith's strongest attack on monopolies was aimed at the entire system of mercantilism and protectionism in foreign trade. In his words, "Monopoly of one kind or another, indeed, seems to be the sole engine of the mercantile system."[10] And, "It is the industry which is carried on for the benefit of the rich and the powerful, that is principally encouraged by our mercantile system. That which is carried on for the benefit of the poor and the indigent, is too often, either neglected, or oppressed."[11] And further, condemning mercantilism on moral grounds,

> To hurt in any degree the interest of any one order of citizens, for no other purpose but to promote that of some other, is evidently contrary to that justice and equality of treatment which the sovereign owes to all the different orders of his subjects.[12]

These lessons were well heeded in the latter eighteenth and early nineteenth centuries by many citizens, and, as history reveals, one of the causes of the American Revolution was the attempt by the British government to enforce the Trade and Navigation Acts, which were intended to monopolize certain activities for Englishmen living in the British Isles.

Modern Trade Restrictions

Unfortunately, the modern-day mercantilists have succeeded in diverting the public's attention away from this reality, and in imposing a vast array of "neomercantilist" policies of trade restrictions. Perhaps the most regulated activity in the U.S. economy is transportation, which serves as an example of monopolies recently created by government.[13]

The Interstate Commerce Commission (ICC) limits the number of firms allowed to engage in common carrier transportation. In addition, it actually sets minimum rates below which transportation companies are not allowed to sell, which permits the companies to enforce a cartel pricing arrangement.

The Civil Aeronautics Board (CAB) has set minimum air cargo rates and passenger rates. It has even attempted to regulate the service provided at these rates to prevent one airline from offering a more comfortable seat or more legroom at a given price than another.

The Federal Maritime Board forces steamship lines into the ocean conferences—the privately operated cartels that regulate ocean freight rates and attempt to prevent rate cutting.

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Forty states regulate intrastate trucking and prevent rate cutting, and most cities regulate the taxicab business, with the same result. Interestingly, Washington, D.C., home of many of the regulators, is the only major city in the U.S. where one can enter the taxi business simply by demonstrating that the necessary liability insurance is covered. Taxi fares in Washington are among the lowest of all major cities in the U.S.

In sum, government regulation of industry is today, as it was in Adam Smith's time, often for the benefit of the regulated firms, to the detriment of consumers, potential competitors, and workers who are barred from employment by the various licensing restrictions which exist and apply to thousands of trades, from taxi driving to fortune telling and the practice of medicine.[14] Only with the sanction and coercion of government can a producer, if a monopolist, reduce output and raise prices *indefinitely*. If the government does not prohibit competition, any monopoly profits will soon be bid away by competing entrepreneurs and workers. The free economy is incompatible with the existence of monopoly power.

Profit Management vs. Bureaucratic Management

As mentioned above, one of the most basic virtues of the free economy is that the market induces private sector entrepreneurs to produce goods and services at least cost. Private sector managers are the residual claimants to both profits and losses—cost reducing innovations which increase profits often lead to direct salary increases and enhance one's human capital as a manager, while economic losses cause one to forgo salary increases and run the risk of losing one's job tenure. In sum, the private sector manager is motivated by both the carrot and the stick, in that he is rewarded financially and promoted for reducing costs, and may be "punished" for unsatisfactory performance.

By contrast, many goods and services which are produced by private sector producers are also provided by government enterprises in many countries. As history shows, government-operated enterprises in both democratic and non-democratic countries have been monumental failures when compared to private enterprise. The effects of bureaucratic (government) management have long been recognized. For example, nearly four decades ago Ludwig von Mises began his book, *Bureaucracy* in the following way:

> The terms, *bureaucrat, bureaucratic,* and *bureaucracy* are clearly invectives. Nobody calls himself a bureaucrat or his own methods of management bureaucratic. These words are always applied with an opprobrious connotation. They always imply a disparaging criticism of

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persons, institutions, or procedures. Nobody doubts that bureaucracy is thoroughly bad and that it should not exist in a perfect world.[15]

The "bureaucratic methods" that Mises referred to are familiar to everyone. Less clear is why these methods persist. The basic reason is not that government bureaucrats are innately lazy, slothful, or dishonest, but that both the carrot and the stick are missing from the public sector. The public manager who reduces cost receives no reward, for there are no profits, by definition, in the public sector. In addition to this, it is difficult to terminate government employees for poor performance, as the low rates of employee turnover in the public sector attest. The manager of a government bureau has, at best, minimal incentives for economic efficiency. In fact, the incentive system facing government bureaucrats in the U.S. and in most democratic European countries is rather perverse, for as Gordon Tullock observed, ". . . in most American and European bureaucracies . . . a bureaucrat is rewarded for simply increasing the number of persons he supervises."[16]

Increased Spending Increases Bureaucratic Power

The budgets allocated by the legislative sponsors of government bureaus are typically exhausted by spending on perquisites of office, salaries of subordinates, and so forth. If the bureaucrat serves his own interests, he will always spend the entire budget allocated to his bureau, regardless of the cost of providing the service which is under his management. Promotions, prestige, and salary increases depend largely on increasing the number of subordinates, which requires an increase in the appropriated budget. The bureaucrat would find it difficult to justify budget increases next year if he does not spend his entire budget this year, and for this reason government enterprises tend to *maximize* rather than minimize production costs, as do their private sector counterparts.

Relative to the private sector, the incentive structure of the bureaucratic "public" manager is perverse, since every bureaucrat is inherently an empire builder who seeks to enlarge the size and scope of his agency in order to increase his salary and prestige. Unlike the private sector, where the managers and owners of inefficient firms bear the burden of poor performance themselves by forfeiting profits, a government-owned monopoly, which most government enterprises are, can not only charge a monopoly price and exhibit gross inefficiencies, but can also force *taxpayers* to pay the price. Government-operated enterprises therefore pose a major threat to the free economy and to personal freedom.

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The Myth of Stabilization Policy

Despite all the world's dismal experiences with attempts at replacing the market economy with "central planning," the dream of many an interventionist is to institute some form of "planning" in the U.S. That is, what is politically defined as "economic planning" is actually the "forcible superseding of other people's decisions by government officers."[17] It is often lamented that planning is needed to protect the public from "accident, chance, and uncoordinated institutions" which lead to "helplessness" as the economy lists.[18] Central planning is seen as simply a matter of "technical coordination by experts" using "systematic analysis" whereby some undefinable "public interest" can be discussed along with "objective analysis . . . of what is really desirable."[19]

Although the U.S. has never actually experimented with *comprehensive* central planning, monetary and fiscal policies since the 1940s have been hybrid attempts at "fine-tuning" the economy by small groups of planners. This predominant approach to economic policy, usually referred to as "Keynesianism," takes as its point of departure a philosophy similar to that described in the above quotations of Nobel prize-winning economist Wassily Leontief and the late Senator Hubert Humphrey. "Stabilization policy," as a form of planning, is merely a matter of getting the "right" people into office, and providing them with adequate technical information. In other words, this view is based on the presumed existence of a group of benevolent and omniscient despots.

It is now widely recognized, however, that the so-called stabilization policies of the past have not worked, and have even *destabilized* the economy.[20] One reason for this is that it is simply impossible to forecast the effects that changes in monetary and fiscal policies will have on an economy 2 years, 1 year, or even 6 months in the future with much precision, as the performance of economic forecasters demonstrates. A second reason is that in a democratic country, the time lag between the recognition of a problem (high inflation, unemployment) and the final impact of whatever policy is implemented to address the problem is unpredictable, due to political realities. A policy aimed at stimulating demand may not actually be felt until after the economy has emerged from a recession and entered into an inflationary peak of the business cycle, which would only make things worse. The failures of government stabilization policies have been described, by their architects, as the result of simply not having sufficient information at hand.

But there is a strong basis for believing that stabilization policies

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have not worked simply because it is not in the interest of policymakers to make them work. For example, expansionary policies (such as government spending financed by money creation) increases political support by dispensing benefits on concentrated constituent groups now, and dispersing and deferring the costs, in the form of higher inflation, in the future. Federal politicians have every incentive to *create* inflation and the further economic instability (stagflation) which follows, especially since the "progressive" income tax (a phrase coined by Karl Marx) generates additional increases in real tax revenues with inflation-induced "bracket creep."

Policies Modified in Proximity to Elections

Relatedly, there is good reason to believe that economic policy is based not on any long-term stability goals, but rather on the proximity to elections, which creates further instability. The theory of the "political business cycle" holds that by concentrating expansionary policies before an election, the incumbent party may be able to strengthen its electoral prospects.[21] Expansionary policies will tend to be pursued more vigorously before an election, with the pursuit of contractionary policies left to after an election, the result being economic instability. In sum, it is the government's monopoly power over the money supply coupled with the pursuit of political self-interest which often creates economic instability.

The predominant view of the failures of stabilization policy, which is informed by what one might call a "central planning mentality," is *not* that existing institutions create incentives for policymakers to generate economic instability, but that such failures are simply the result of accident or error. Economist Herschel Grossman, in reviewing the work of James Tobin, one of the chief architects of Keynesian economics over the years, summarizes this view:

> Tobin presumes that the historical record of monetary and fiscal policy involves a series of avoidable mistakes, rather than the predictable consequences of personal preferences and capabilities working through the existing constitutional process by which policy is formulated. Specifically, Tobin shows no interest in analysis of either the economically motivated behavior of private individuals in the political process or the behavior of the government agents who make and administer policy.[22]

In essence, the predominant view of stabilization policy, like the socialist dream of the centrally planned economy, is based on a vision of a utopian society run by angels who automatically serve the public interest (however defined), and there is no agency problem. But if one accepts the notion that policymakers

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are human beings, and therefore act in their own self-interests, it becomes necessary to face the question of why governments would pursue *any* of the competing goals of monetary and fiscal policy. As economist Paul Craig Roberts stated,

> What do policymakers, especially in a democratic political system, have to gain from an efficient, stable economy that is maximizing social welfare? Such a successful economy would cut into their abilities, as entrepreneurs, to build the spending and regulatory constituencies that are the basis of their political power. If people can get ahead through the market, and the tax system allows them to accumulate wealth, what happens to the demand for all the welfare handouts, food stamps, housing subsidies, and income security programs? Without all these programs, what would government do? How would politicians carry on their demagogy and set group against group, class against class, and race against race if the tax system were actually used to bring about an equal distribution of income and wealth?[23]

There is certainly much evidence of this. How else can one explain the extreme opposition by entrenched government bureaucracies to supply-side economics which attempts to restore incentives to work and invest and to alleviate poverty by the only means known to man—stimulating economic growth and wealth creation in the private sector? In short, those who benefit from public sector expansion have found it essential to undermine the activities of and public confidence in the private sector.

Stabilization policy, a watered-down version of central planning, has served, and will continue to serve to destabilize the private sector of the economy and to transfer resources and power to the government. After all, why should one expect government bureaucrats to solve the problems which justify their very existence? While the free economy may not be void of economic fluctuations, government attempts at "fine-tuning" have only destabilized the economy even more than what would have otherwise taken place, and will continue to do so as long as they are used.

Conclusions

The free economy is most conducive to maximizing consumer welfare, as defined by consumers themselves. In the free economy it is ultimately the consumer who determines the pattern of production and distribution, the distribution of income, and induces entrepreneurs to produce goods and services at least cost. It is precisely for these reasons that interventionists are so opposed to the free economy. When political resource allocation replaces the market allocation of resources the result can only be the forceful imposition of the preferences of governmental agents for those of con-

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sumers, which is neither efficient nor equitable.

Political resource allocation, relative to the market, is wasteful and severely limits individual freedom and welfare. Furthermore, attempts at "fine-tuning" or "planning" are nothing more than attempts to subjugate consumers and taxpayers to the preferences of those who have seized political power, and have severely reduced the wealth of nations. As a glance at any map of the world reveals, only the free economy is capable of achieving equity and prosperity.

—FOOTNOTES—

[1]Ludwig von Mises, *Human Action: A Treatise on Economics,* 3rd Ed., (Chicago: H. Regnery Co., 1966), p. 270.

[2]Milton and Rose Friedman, *Free to Choose: A Personal Statement* (New York: Harcourt Brace Jovanovich, 1979), p. 13.

[3]James Madison, *The Federalist,* 10.

[4]Alexander Hamilton, *The Federalist,* 6.

[5]James Madison, *The Federalist,* 51.

[6]James M. Buchanan, "Why Does Government Grow?" in T. Borcherding, Ed. *Budgets and Bureaucrats: The Sources of Government Growth,* (Durham, N.C.: Duke University Press, 1977), pp. 3–18.

[7]Jerome Rothenberg, *Economic Evaluation of Urban Renewal* (Washington, D.C.: Brookings Institution, 1967), p. 65.

[8]This is a dominant theme of the economics of bureaucracy. See, for example, William Niskanen, *Bureaucracy and Representative Government* (Chicago: Aldine, 1971).

[9]Adam Smith, *The Wealth of Nations,* Cannan Edition, (London, 1960), vol. II, p. 427.

[10]*Ibid,* p. 129.

[11]*Ibid,* p. 143.

[12]*Ibid,* p. 152.

[13]The following examples are cited in Yale Brozen, *Is Government the Source of Monopoly? and Other Essays* (San Francisco: The Cato Institute, 1980).

[14]A detailed discussion of occupational licensing is found in Walter E. Williams, "Government Sanctioned Restraints That Reduce Economic Opportunities for Minorities," *Policy Review,* (Fall 1977), pp. 1–29.

[15]Ludwig von Mises, *Bureaucracy* (Westport, Conn.: Arlington House, Reprinted 1969), p. 1.

[16]Gordon Tullock, *The Politics of Bureaucracy* (Washington, D.C.: Public Affairs Press, 1965).

[17]Thomas Sowell, *Knowledge and Decisions* (New York: Basic Books, 1980), p. 214.

[18]Wassily Leontief and Leonard Woodcock, "The Case for Planning," in *The Politics of Planning,* p. 348.

[19]Hubert H. Humphrey, *National Economic Planning: Right or Wrong for the U.S.?* (Washington, D.C.: American Enterprise Institute, 1976), p. 3.

[20]Even Franco Modigliani, perhaps the chief inventor of Keynesian economics in the U.S. came to this conclusion in his 1977 presidential address to the American Economic Association, "Should We Forsake Stabilization Policies?" *American Economic Review* (May 1977).

[21]See, for example, Richard E. Wagner, "Economic Manipulation for Political Profit: Macroeconomic Consequences and Constitutional Implications," *Kyklos,* vol. 30, (1977), pp. 395–409.

[22]Herschel Grossman, "Tobin on Macroeconomics: A Review Article," *Journal of Political Economy* 83 (August 1975), pp. 845–46.

[23]Paul Craig Roberts, "Taxation and the Induced Demand for Leviathan," paper presented at the 1980 meetings of the Mont Pelerin Society, The Hoover Institution, Palo Alto, California.

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The Subterranean Economy

NOT so many years ago my 35-year-old horse Toy died in the middle of a frozen January. Digging a grave for him in the snow-blanketed ground with ordinary tools was a manifest impossibility. A man with a backhoe, hearing of my plight, offered to do the job for me. I was about to ask his name in order to make out a check for an agreed-upon $100 when he said, "If you have ninety dollars in cash I'll take that."

I don't know whether that $90 ever figured in the Gross National Product, but I have wondered about it. Similarly I wonder about the incomes of all those street hawkers who sell everything from women's handbags to polished red apples in and around Grand Central Terminal in New York City. In businesses where there is little overhead and no documented inventory how much of any given transaction produces a statistic that is recorded?

At the other end of the scale we have computers spewing out thousands of documents that go into files far too voluminous for any correlation. In a suggestive book called *The Subterranean Economy* (New York: McGraw-Hill, 187 pp., $19.95), Dan Bawly, an executive partner of an Israeli certified public accountant firm, says that Americans produce 72 billion documents annually. There are, so Bawly tells us, approximately 18,000 papers for every white collar worker in the United States, and the total number of records, vouchers and other documents on file must exceed three billion.

As an international accountant with business in Europe, America

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and the Middle East, Mr. Bawly has good reason to believe that no Gross National product statistics are reliable. Between unrecorded transactions, mislaid files and untotalled slips of paper, the job of making a science of macroeconomics becomes a joke. In computer language, it's "garbage out."

Just Getting Even

There can be no science without measurement, said Lord Kelvin, and Mr. Bawly would be the first to admit that *The Subterranean Economy* is not a scientific book. But he is satisfied in his own mind that, with the proliferation of tax-consuming and inflation-creating welfare state bureaucracies, thousands of individuals have come to regard their political representatives as crooks. Tax evasion is no longer regarded as immoral; it's just getting even.

To describe the new attitude, Arthur Seldon of the Institute of Economic Affairs in London has coined a new word. It is "avoision," compounded of "avoidance" and "evasion." Tax avoidance has always been legitimate. But now Mr. Seldon sees a moral blurring of avoidance and evasion. The higher the tax rate, the more popular the "avoision" schemes.

The Gross National Product statistics either underreport or totally exclude many activities that should be relevant to any meaningful science of human action. Mr. Bawly lists a few of these activities. There is, first of all, moonlighting. In both Europe and the United States there is the illegal employment of aliens. Barter is a big item. There is tax evasion through manipulated expense accounts. And there are the myriad "laundering" activities related to the dope traffic and the cultivation, in California and Hawaii, of big unrecorded cash crops of marijuana. Money from heroin, cocaine and marijuana passes from hand to hand and into bank accounts for subsequent "laundered" investment in legitimate business. And where is the farmer who is meticulous about recording roadside stand sales? In parts of Canada, for example, the unrecorded exchange of farming, fishing and forestry commodities only rarely leaves an audit trail the Ottawa government can pick up.

The "guesstimates" of the extent of the American underground economy naturally vary. *Fortune* magazine has figured that $50 billion a year in taxes are lost to government. In 1976 the Internal Revenue Service said the covert economy was approximately one-tenth of the surface economy. In 1981 the Department of Labor estimated that nearly one in twenty workers held more than one job during a particular survey period. Presumably, much of the "moonlight" income went unreported. The General Accounting Office has estimated that some $30 bil-

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lion in taxable income remains "off the books," which means a substantial loss in annual Federal income taxes.

The probability is that government estimates of the underground economy err on the conservative side. If "authorities" were to admit their inadequacy to the job of tracking down every unrecorded dollar, it might encourage more people to be more brazen about practicing "avoision." Police state measures would then be necessary, and the American people wouldn't stand for that.

Tax Avoidance Is Common In Other Countries

In other countries there is less reticence in speaking about "avoision." Despite the recent jailing of Sophia Loren on a tax evasion charge, the Italians boast that their underground economy has saved the nation from collapse. In spite of the fact that the Italian government in 1978 was close to bankruptcy, the country imported more Rolls-Royce cars and caviar than any other Common Market nation. It was second only to Britain in its consumption of French champagne. There is much less labor unrest in Italy's clandestine businesses than in the open economy, where the Communist unions are strong. The presence of moonlighting in Italy gives the entrepreneur access to a flexible labor force that is willing to work overtime. There is no registered glove factory in Naples, yet this city exports five million pairs of gloves annually. The unmeasured Naples shoe industry is supposed to be just as large as the glove industry.

Macroeconomic data in Italy are meaningless. Things are not much different in France, where a quarter of the 25 million labor force is thought to be in moonlighting. Unrecorded labor in France has, says Mr. Bawly, contributed materially to the construction of highrise buildings in cities from Paris to Nice. Pay in the unrecorded economy goes up, with the employer and the employee sharing the amount of tax avoided between them.

In supposedly moral Britain the "unmeasured" economy is estimated as 7.5 per cent of the surface economy. Scotland reports an unemployment rate of ten per cent, but the London *Economist* suspects the figures. The "largest industry north of the border," says the *Economist,* "lies in the penumbra of services relating to providing Bed and Breakfast, and most of them avoid the taxman's eye." And the illicit whisky still in Scotland has always been a healthy sector of highland output. As for fish, "far more are landed than are officially sold."

The underground economy, says Bawly, will continue to grow until the Welfare State is cut back. It is as simple as that.

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The Illusion of a
Riskless Society ..... Elgin Groseclose 464

Rothbard's Liberty Reviewed .... John Hospers 468

Mixed Economies a
No-Man's Land ..... Glenn L. Pearson 485

Public Policy and the
Free Economy ..... T. J. DiLorenzo 492

BOOKS

The Subterranean Economy ..... John Chamberlain 510

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